

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petitions	:	
of	:	
CAROL A. GROH AND DONALD C. SMITH	:	DETERMINATION
for Redetermination of Deficiencies or for Refund of	:	DTA NO. 810532
New York State and New York City Income Taxes under	:	AND 813342
Article 22 of the Tax Law and the New York City	:	
Administrative Code for the Years 1986 through 1991.	:	

Petitioners, Carol A. Groh and Donald C. Smith, c/o Robert Plautz, 330 Madison Avenue, New York, New York 10017, filed petitions for redetermination of deficiencies or for refund of New York State and New York City income taxes under Article 22 of the Tax Law and the New York City Administrative Code for the years 1986 through 1991.

A hearing was held before Thomas C. Sacca, Administrative Law Judge, at the offices of the Division of Tax Appeals, 500 Federal Street, Troy, New York, on January 25, 1995 at 11:00 A.M., was continued at the same location on January 26, 1995 at 10:15 A.M., January 27, 1995 at 9:30 A.M., July 24 and 25, 1995 at 11:00 A.M., July 26 and 27, 1995 at 9:30 A.M., February 5, 1996 at 10:00 A.M., February 7, 1996 at 9:30 A.M. and was continued to conclusion at the same location on February 8, 1996 at 9:30 A.M. Petitioners' brief was filed on April 22, 1996. The Division of Taxation filed its brief on July 22, 1996 and petitioners' reply brief was filed on August 15, 1996, which date began the six-month period for the issuance of this determination. The six-month period was extended for an additional three months, pursuant to Tax Appeals Tribunal Rules of Practice and Procedure § 3000.15(e)(1). Petitioners appeared by Robert Plautz, Esq. The Division of Taxation appeared by Steven U. Teitelbaum, Esq. (Craig Gallagher and Donna M. Gardiner, Esqs., of counsel).

ISSUES

I. Whether petitioners were domiciliaries of the City and State of New York for the years 1986 through 1991 and were thus taxable as resident individuals.

II. Whether petitioners were statutory residents of the City and State of New York for the years 1986 through 1989 and were thus taxable as resident individuals.

III. Whether petitioners have established that they incurred ordinary and necessary business expenses within the meaning and intent of Internal Revenue Code § 162 for the years 1986 through 1991.

IV. Whether petitioners have established that they are entitled to deductions for certain charitable contributions claimed for the years 1986 and 1987.

V. Whether petitioners incurred a capital loss under Internal Revenue Code § 1231 upon the sale of 848 shares of stock held in a cooperative apartment at 212-214 East 77th Street, New York, New York in the year 1987.

VI. Whether petitioners properly deducted losses from their passive activities pursuant to Internal Revenue Code § 469 for the years 1988 and 1989.

VII. Whether petitioners substantiated the amount of the casualty loss claimed to have been caused by Hurricane Hugo in the year 1989 within the meaning and intent of Internal Revenue Code § 165.

VIII. Whether petitioners incurred investment interest expenses pursuant to Internal Revenue Code § 163 for the years 1988 and 1989.

IX. Whether petitioners were deprived of their fundamental rights to due process and to confront their accusers by the absence from the hearing of the individuals who conducted the audits for the years 1988 through 1991.

X. Whether the notices of deficiency for the years 1988 through 1991 are supported by "substantial evidence" within the meaning of State Administrative Procedure Act § 306(1) and, if not, should be cancelled.

XI. Whether petitioners have established reasonable cause for the abatement of penalties imposed pursuant to Tax Law § 685(b)(1) and (p).

FINDINGS OF FACT

1. Petitioner Donald C. Smith was born in Fostoria, Ohio in the year 1929. In 1959, he

graduated with a B.S. degree in architecture and in 1961 he received a masters degree in architecture from the University of Pennsylvania. After graduating from the University of Pennsylvania he sought employment with Skidmore Owings & Merrill ("Skidmore"), one of the world's largest architectural firms. Skidmore was then and continues to be headquartered in Chicago, Illinois. Mr. Smith was hired by Skidmore in 1961 and assigned to work in its New York City office. He began as a draftsman in that year, was elected a participating associate in 1963, an associate partner in 1965 and was made a full partner in 1969. Mr. Smith was a member of Skidmore's Partners Committee which directed the affairs of the firm. The meetings of the committee were held in Chicago, New York and San Francisco.

In the 1960s and early 1970s, Mr. Smith spent most of his time working for the firm either in New York or in Edmonton, Canada. In New York, he designed and built, among other projects, the General Insurance Company building in Greenwich, Connecticut and New York University's Business School in lower Manhattan. In Edmonton, he worked with a developer named Don Love in designing and building six major commercial towers of between 35 and 45 stories in the downtown area.

2. Petitioner Carol Groh was born in Grand Rapids, Michigan. She attended Hillsdale College in Michigan and later transferred to the Parsons School of Design in New York City. Ms. Groh graduated from Parsons in 1966 with a B.A. degree in environmental design. In 1968, she accepted employment as an interior designer in the New York City office of Skidmore Owings & Merrill. Petitioners met in 1972 while both were working for Skidmore in New York City, and were married in 1976.

3. In 1964, Mr. Smith purchased and resided at 211 East 62nd Street, New York, New York. He sold the property in March 1977. Petitioners' certified marriage license in 1976, as well as the certified birth certificate of their first son, born in 1977, indicated their residence to be 251 East 51st Street, New York, New York. While the record is unclear as to when, if ever, petitioners disposed of the 51st Street apartment, the record is clear that, by January 1978, petitioners already owned and had telephone service at their apartment located at 175 East 62nd

Street, New York, New York. The certified birth certificate of their second son born in 1981 listed their residence to be 175 East 62nd Street. Furthermore, it is undisputed that petitioners owned and maintained this apartment throughout the audit period.

4. In 1972, Don Love approached Mr. Smith to request that he join him in various projects concerning the construction and development of downtown Denver, Colorado. Mr. Smith accepted the offer because he saw a large amount of opportunity there. He requested that Skidmore open an office in Denver with himself as the partner-in-charge. Mr. Smith would serve as the architect in charge of design as well as the architect in charge of management and construction of the Denver office. In 1972, Mr. Smith and Ms. Groh started the Skidmore Denver office and by 1974, the office had 60 employees.

Initially, petitioners rented an apartment on Humboldt Street in Denver. In 1977, they purchased a home in Denver at 385 Gilpin Street which they sold approximately one year later. Following the sale of their house they again rented an apartment in Denver at 1077 Race Street. The apartment's square footage was 3,000 square feet.

5. During the mid-to-late 1970s, Mr. Smith began to work with another real estate developer in Denver named John Whitney. Mr. Smith designed and built two office buildings for Mr. Whitney in Denver, the 36-story Denver National Bank Building and the 47-story 17th Street Plaza. In 1976 Ms. Groh was forced to resign from Skidmore because the firm had a policy against employees being married to partners. After resigning, she began developing her own interior design business and did the interior design work on the buildings for Mr. Love and Mr. Whitney. Ms. Groh did the interior design work on the same buildings on which Mr. Smith did the exterior and structural architectural design work. Ms. Groh also joined with another former employee of Skidmore's New York City office to form an interior design firm, GN Design Associates, Inc. ("GN Design"), initially located in an apartment on East 51st Street in Manhattan. The firm later moved its offices to a building located at 57th Street and Madison Avenue. The partnership was dissolved in 1988.

6. The 1986 corporate franchise tax return of GN Design, stated that it was a New York

corporation which began doing business in New York in January 1979. Likewise, an article in the August 1987 edition of Working Woman magazine stated that GN Design was based in New York in January 1979. An article from Business Week for June 1988 stated that GN Design was located on Manhattan's East Side in 1979. Finally, an article in the Washington Post from January 1988 stated that "New York interior designer Carol Groh of GN Associates" had been named designer of the year.

7. During 1976, Mr. Smith was approached by Mr. Whitney to join him in the development of a two-block area in downtown Denver entitled the Tabor Center. The proposal was for Mr. Smith and Skidmore to be involved in the project not only as architects, but as financial partners as well. Skidmore rejected the offer as it wished to remain exclusively in the business of supplying architectural services. However, the firm did not have any objection to Mr. Smith, on his own, joining with Mr. Whitney on the project. Mr. Smith therefore joined Mr. Whitney, providing his architectural skills and \$25,000.00 in exchange for a 50% interest in the Tabor Center. This was the first of many projects which involved Mr. Smith, on his own, investing substantial sums of money and time in developing, designing and assisting in the management of commercial real estate ventures throughout the United States. Others included the following:

- a. 33 West Monroe Street, Chicago, Illinois - a 38-story office building in which Mr. Smith personally invested \$60,000.00.
- b. 46 North Michigan Avenue, Chicago, Illinois - a 46-story apartment building in which Mr. Smith invested \$250,000.00.
- c. 333 Bush Street, San Francisco, California - a 62-story building in which Mr. Smith invested \$50,000.00.
- d. Symphony Towers, San Diego, California - a 46-story office tower with a 450-room hotel in which Mr. Smith invested \$60,000.00.
- e. Pinehurst Apartments, Dayton, Ohio - an apartment complex in which Mr. Smith invested \$60,000.00.

- f. Riverside Apartments, Dayton, Ohio - an apartment complex in which Mr. Smith invested \$10,000.00.
- g. Highland Commons, Tampa, Florida - a 94-story office tower and shopping center in which Mr. Smith invested \$250,000.00.
- h. Valley Hill Associates, Tarrytown and Kew Gardens, New York - Mr. Smith invested \$250,000.00.
- i. 212-214 East 77th Street, New York, New York - an apartment building in which Mr. Smith invested \$950,000.00.
- j. 22-24 West 69th Street, New York, New York - an apartment building in which Mr. Smith invested \$50,000.00.
- k. 106 West 69th Street, New York, New York - an apartment building in which Mr. Smith invested \$250,000.00.
- l. 345 Park Avenue, New York, New York - an office tower in which Mr. Smith brought the respective parties together as a joint partner with other partners of Skidmore.

After 1987, petitioners made no further business investments in New York City or State, generally limiting their investments to St. Croix and Denver, Colorado.

Ms. Groh was also actively involved in many of these projects. While Mr. Smith designed the buildings, she handled the interior designing and design work such as public space design for lobbies and tenant corridors in the apartment buildings. Ms. Groh would also specify and select the materials, finishes, furniture and fixtures associated with the interior requirements.

8. Both petitioners testified that, at the time of their marriage in 1976, they were domiciled in Denver, Colorado. Contrary to petitioners' testimony, the certified copy of the marriage license stated that Donald Smith's place of residence at the time of their marriage was 251 East 51st Street, New York, New York. Carol Groh's place of residence was listed as 251 East 51st Street, New York, New York.

Both Mr. Smith and Ms. Groh testified that they were married on a tall ship which was

sailing on the high seas, out of the jurisdiction of New York State. Ms. Groh stated it was a legal marriage and that they did not have to memorialize their marriage in any way on land. Contrary to petitioners' testimony, the certified copy of the marriage license, as indicated in the portion of the license entitled "To Persons Performing Marriage Ceremony", stated that the officiant of said ceremony was Gilbert Rabin, City Justice, and that he performed the marriage at his home in Yonkers, New York at 10:35 A.M. on July 17, 1976.

9. Petitioners testified that in 1977 they resided in the State of Colorado. During that year, petitioners' first son was born in New York City. Ms. Groh explained that during the first few months of the pregnancy she would speak to the doctor on the telephone to assure him that she was eating properly. As there was a Down's Syndrome child in Mr. Smith's family and Ms. Groh had become pregnant with her first child at a later age in life, she had amniocentesis performed at the Columbia Presbyterian Hospital in New York City in her 16th week of pregnancy. From this point forward, she would come to New York once a month to see her doctor, staying one or two days each visit. As the term of the child drew near, petitioners set up a date with their doctor in New York for the birth of their child. Ms. Groh was to fly to New York two days before the scheduled delivery date and stay with a friend in Manhattan. On the date chosen, delivery would be induced, and Ms. Groh would return to her friend's apartment after one or two days in the hospital. Following the birth of their child, Mr. Smith returned to Denver, Colorado or some other place of business. During the two to three days of recuperation spent at her friend's apartment, Ms. Groh was attended to by her mother and Mrs. Nellie Gomes, a nanny hired by petitioners immediately before the birth of their first child. After approximately one week of Ms. Groh's time spent in New York, Mr. Smith returned to New York and he, along with Ms. Groh, the baby and Mrs. Gomes returned to Denver. The birth of petitioners' second child was accomplished in much the same way.

Contrary to petitioners' testimony, the certified copy of the birth certificate of their first son stated that the mother's usual residence was 251 East 51st Street in New York City. The birth certificate further stated that, pursuant to the Bureau of Vital Records, Department of

Health, City of New York, the mailing address of the mother was "Mrs. Carol Smith, 251 East 51st Street, Apt. 20-M, New York, New York 10022."

Petitioners testified that in 1981, the year of the birth of their second son, they resided in the state of Colorado. Contrary to petitioners' testimony, Ms. Groh listed her usual residence on the birth certificate as being in New York City, but this time, her New York City address was the 175 East 62nd Street apartment. The birth certificate further stated that, pursuant to the Bureau of Vital Records, Department of Health, City of New York, the mailing address of the mother was, "Mrs. Carol Smith, 175 East 62nd Street, New York, New York 10021."

10. Mr. Smith testified that at the time he and his wife were in Denver, neither he nor his wife had a permanent place of abode in New York. Both petitioners confirmed on cross-examination that neither maintained a permanent place of abode in New York during the years that they were in Denver.

There was no documentation submitted, other than a letter from the state of Colorado concerning petitioners' filing of Colorado tax returns for the years 1976 through 1981, to establish that they resided in Colorado during any period of time. In fact, the letter does not state from which address petitioners filed their state returns. Although petitioners claimed to have moved to Colorado in 1974 and to have filed resident returns from 1974 through 1981, they did not file as residents of Colorado for either 1974 or 1975.

11. Mr. Smith testified that in 1981 the senior partners of Skidmore requested that he return to New York to become the partner-in-charge of the New York office. Mr. Smith decided to return to New York with one of the conditions being that he would have full access to Skidmore's limousines and drivers for his and his family's daily needs. There were four Skidmore drivers assigned to the New York City office. This would allow petitioners and their sons to live outside New York City with easy access to work for petitioners and to school for the children within the City. Mr. Smith testified that in the winter of 1982 the whole family left Denver and moved back East.

In accordance with these plans, in December 1982, petitioners bought an eight-room,

four-bath, two-car garage house located on Lake Mohawk in Sparta, New Jersey. The house was situated on one acre of land. The purchase price was \$190,000.00 and financing for the purchase was obtained from the National Community Bank, a local bank in Sparta. On April 4, 1983, petitioners moved the furnishings from their apartment in Denver to their house at 518 West Shore Trail, Sparta, New Jersey. However, petitioners filed as New Jersey residents for the entire 1982 tax year. The certified copy of the deed to the Sparta house listed petitioners' address as 175 East 62nd Street, New York, New York.

12. For approximately three years following the purchase of the Sparta house, petitioners made \$321,160.60 worth of improvements. The kitchen was gutted and expanded with all new equipment and appliances added. The outdoor porch was enclosed with a full glass wall and made into a ninth room. Petitioners moved the garage and the driveway from the back of the house to the side of the house, in the process creating an outdoor deck. An outdoor heated pool was added along with a trampoline. Petitioners also put in a new heating system and added central air conditioning.

According to petitioners, their home in Sparta was furnished with expensive and rare contemporary furniture and paintings. Among other items, it had paintings by Franz Klien and Claes Oldenberg, the latter painting appraised in 1989 at \$70,000.00. The house also had Eskimo art work and furniture designed by Herman Miller. In addition, the house contained a dining room table designed by Ms. Groh.

Petitioners maintained a homeowners insurance policy for their house in Sparta with State Farm Fire Mutual Casualty Company, and it specifically included an additional rider for jewelry, furs and artwork in the Sparta house. There was no such rider for the apartment that they maintained in New York City at 175 East 62nd Street.

13. Immediately after moving to Sparta, Mr. Smith bought a Scorpion speed boat for water skiing on the lake that abutted their property. The boat was registered and moored in Sparta. In 1987, Mr. Smith traded in the Scorpion boat for a new 19-foot Master Craft inboard boat. The Master Craft was also used for water skiing on the lake and was registered and

moored in Sparta.

During the audit period, Mr. Smith had a driver's license from the State of New Jersey. In 1987, Mr. Smith bought a new Chevrolet Blazer and registered it in New Jersey where it remained registered until 1992. All other vehicles owned by Mr. Smith during the audit period were registered in St. Croix. Ms. Groh's Jaguar was also registered in New Jersey. However, she maintained her New York State driver's license throughout the audit period.

14. Petitioners testified that their social and family life was centered in Sparta from 1982 through most of the audit period. The children's doctors were located in Sparta. With rare exception, every weekend was spent in Sparta. Each July 4th Holiday, a family reunion of Mr. Smith's relatives was held in Sparta. During the warm weather, weekends were spent water skiing and swimming in the pool. In the winter, the lake would freeze over and the children would ice skate and play hockey and sleigh ride on the local golf course. While the family lived in Sparta, they did not go to Central Park, the movies, professional baseball or basketball games, museums, Broadway shows or the ballet in New York City. Petitioners were members of two country clubs in Sparta, the Lake Mohawk Country Club and the Lake Mohawk Golf Club. They were not members of any social clubs in New York.

15. Petitioners' sons attended The Allen-Stevenson School located in Manhattan from 1983 through 1992. The residence of record for petitioners' sons, as listed with the school, was 175 East 62nd Street from 1983 to the end of 1991. For the school years 1985-1986 and 1986-1987, Mr. Smith was co-chairman of the Parents Committee for the annual fund drive for The Allen-Stevenson School.

16. According to Mr. Smith, the children spent all of their nonschool days in Sparta during the years in question. While discussing his 1986 diary, Mr. Smith testified that he and his family stayed in Sparta every time that they had the chance. "That is our home and that is where our kids wanted to be and grow up in Sparta." Mr. Smith testified that from 1986 to 1991, he generally spent weekends in Sparta. Petitioners claimed that after 1985 Nellie Gomes spent 1 month in St. Croix and the remaining 11 months in Sparta, always staying with the

children. Furthermore, Mr. Smith stated that "[m]y home in 1986 was in Sparta, New Jersey." These statements contrast with petitioners' original claim that they were domiciled in St. Croix beginning in 1985.

17. Petitioners' Exhibit "7" was described by Mr. Smith as follows:

"Exhibit '7' is a series of six pictures marked A to F which illustrate the house in the wintertime, roughly '84; they were all taken at the same period of time. And it illustrates quite vividly the look of the house from the front, from the rear, from the yard and its relationship to the lake and its improvements that we made in the early years to the house at 518 West Shore Trail after purchasing it in 1982."

With respect to photo B, the date on the back of the picture is March 1992.

Although there were several pictures depicting the outside of the New Jersey house, there were no photos of the interior of the house during the years 1984 through 1992.

18. In 1985, Mr. Smith began to consider his retirement from Skidmore. Skidmore had a mandatory retirement age of 65 but Mr. Smith planned on leaving in 1989 at age 60. In anticipation of retirement, he decided to begin developing new business opportunities that he would find both invigorating and challenging. To that end petitioners investigated the United States Virgin Islands for opportunities to build and develop property. On the island of St. Croix, petitioners paid \$1,000,000.00 in cash for an unimproved 13-acre beachfront parcel of land named Green Cay. The transaction occurred on August 9, 1985.

Following the purchase, Mr. Smith began to develop the Green Cay property. He cleared the land, installed a fresh water well, put irrigation lines into place and planned their beachfront house. Petitioners also began the process of subdividing a portion of Green Cay.

Approximately four months later, petitioners were shown another piece of property entitled Annas Hope. They immediately realized that while Green Cay was well suited for the purpose of developing residential sales, Annas Hope provided a better location for their personal residence. In addition, petitioners planned on renovating three of the four houses presently on Annas Hope which would mean starting a second business on St. Croix of renting luxury vacation units. On April 1, 1986, petitioners bought Annas Hope for \$1,060,000.00 in cash. It is noted that petitioners never resided at Green Cay.

19. Annas Hope is a 6-acre peninsula with a cliff 23 feet above sea level that juts out into the Caribbean Sea. Following the sale, petitioners tore down the one building that was at the point of the peninsula and began to convert the three remaining units into rental units. Petitioners did extensive landscaping to the six acres of Annas Hope. They built a new road to the property and planted more than 2,000 sea grape trees, dozens of Christmas palms, hundreds of Hibiscus plants and many more plants including Alamanda and Bougainvillea. They also planted a small orange and grapefruit orchard. The cost for the landscaping performed by petitioners during the years 1986 through 1988 was approximately \$473,000.00. Petitioners never used the rental units for their own personal use, but instead resided in a home located at 35 Green Cay which they rented during their visits while their residence on Annas Hope was being completed. For instance, petitioners and their children went to St. Croix for the Christmas vacation of 1986, renting the 35 Green Cay home while they were there.

The house designed and built by petitioners is eight rooms with an interior floor space of 5,550 square feet and roof space of 7,000 square feet. Petitioners had a St. Croix construction company, Caribbean Construction Services & Associates, do the labor and supply the basic materials. Construction took almost two years to complete and construction costs for labor and miscellaneous materials from Caribbean Construction as of February 1988 were \$1,468,130.00. This amount did not include the \$491,710.00 paid directly by Scotiabank to Caribbean Construction for work and construction on the three rental units on Annas Hope, pursuant to a construction loan obtained by petitioners. Total payments made by petitioners to vendors of materials not purchased through Caribbean Construction was \$694,000.00. Included in the items purchased directly by petitioners were: 88 tons of Sardinian Grey Granite imported from Italy and used for the walkways surrounding the houses; a flag pole specially equipped with a lightning preventer which neutralized the ions in the air during a storm; a seven-foot diameter butcher block table that measured six inches thick; 60 tons of Ming green marble imported from China and used on the interior floors and the bathrooms; a dining table measuring 15 feet square and 2 kitchen counters measuring 18 feet long, made of dark green Vermont marble; kitchen

cabinets made of French ash; Iroka mahogany imported from Africa to make the interior gables of the house; and special glass and framing for the doors and windows which were needed because of the salt air on the peninsula. Petitioners' house on Annas Hope was first occupied by them in November 1987.

Petitioners hired Henry and June Bogdanik to manage the St. Croix property. The Bogdaniks had check-signing authority on two accounts with Chase Manhattan Bank: the Smith Groh, Inc. account and the Donald C. Smith account. The checks on both accounts were used to cover expenses arising out of the St. Croix property. In 1989, George Tyger replaced the Bogdaniks as manager.

20. The Green Cay property that petitioners purchased for \$1,000,000.00 was in its natural state at the time of the purchase. Immediately after the sale, petitioners began to develop it for sales of residential lots. Petitioners brought in bulldozers and heavy equipment, cleared the land, hired the Roe Win Construction Company in St. Croix to complete the major earth moving efforts and hired two full-time landscapers. They built an irrigation system with a stone container wall and plastic barriers to control the water runoff into the sea. They attempted to drill one well but it was dry, so they drilled a second well to irrigate future plantings. They built a pump house, brought in electricity, built a blacktop road and cleaned up the beach. By April 1987, petitioners had invested an additional \$821,000.00 in the Green Cay property over and above the original purchase price. On April 9, 1987, petitioners sold Green Cay for \$2,500,000.00.

21. During the audit period, petitioners maintained the apartment at 175 East 62nd Street in New York City. The parties agree that the 175 East 62nd Street apartment was a permanent place of abode during the audit period. Petitioners testified that the apartment was purchased in 1978 for \$140,000.00. The auditors also concluded that it was 1978 based on the fact that petitioners had a telephone line connected in that year. The renovations done to 175 East 62nd Street were completed in late 1982 or early 1983, and upon completion petitioners were issued a new share certificate. Petitioners testified that, when the renovations were completed, they did

not sell the apartment for a variety of reasons. The real estate market was weak at this time and petitioners felt they would not get the amount of money they deserved. Mr. Smith also needed an office for his non-Skidmore business dealings which included meetings with potential landowners and clients, having a place to work and keep records and having a place for the part-time employees to work. These part-time employees were involved in developing plans, ordering materials and working with the contractors. Finally, petitioners found the apartment to be a comfortable place to stay overnight when they had business in Manhattan which kept them there late or when the weather made it difficult to return to Sparta.

The total square footage of the apartment after the renovations was approximately 3,000 square feet. The apartment had been totally gutted, including some of the exterior walls. In 1982, petitioners purchased the apartment next door, annexed a room and resold the remaining portion of that apartment. This room served as the children's bedroom. Petitioners testified that the living room of the apartment was used as the office headquarters for Mr. Smith's business activities unrelated to Skidmore. The office contained a secretarial desk, computer, drafting board, conference table with chairs, file cabinets and other office equipment. Introduced into the record of this matter was the floor plan of the apartment and a series of nine pictures which depicted the interior of the apartment and the office equipment previously mentioned. The pictures also show petitioners' bedroom and a couch. What is not shown is the kitchen, the maid's room and the children's room. Mr. Smith testified that although Skidmore principals tolerated his outside real estate business activities, it was necessary for him to have an office outside of his Skidmore office because they did not want him to be performing his private business at their office. However, despite that testimony, there is no question that Mr. Smith billed his travel and entertainment expenses for his personal business through Skidmore expense accounts. Petitioners also testified that the family would sleep overnight in the apartment on those occasions when they might stay late in the City or there was inclement weather. According to petitioners, they averaged approximately three to four overnights in the apartment per month. The 175 East 62nd Street apartment was contracted for sale in 1991 for

\$1,500,000.00 and the closing took place in 1992.

22. On October 9, 1990, the auditors visited the 175 East 62nd Street apartment with Mr. Smith and his representative. According to the auditors, Mr. Smith stated to them that he had moved out of the apartment in 1982. Several of the doors were locked, and the auditors were not shown the kitchen and the maid's room. After obtaining a copy of the apartment's floor plan from the cooperative manager, the auditors met again with Mr. Smith and were reshowed the apartment, including the kitchen and another bedroom.

23. Petitioners introduced six pictures into the record of this matter which, according to petitioners, show the furniture which was situated in their Sparta house. The pictures were taken in their Greenwich, Connecticut house after the Sparta house had been sold. However, it appears from the photographs of the interior of the Greenwich house and the photographs of the interior of the apartment on 175 East 62nd Street that the couch and some of the chairs are the same.

24. Petitioners received mail at their New York address during the years in question including their St. Croix real property tax bills for 1985, 1986 and 1987, their New Jersey real property tax bills, their Chase checking account statements, their Chase mortgage account statements, their National Community Bank (New Jersey) mortgage statements as well as their New Jersey United Telephone bills. All of petitioners' bank accounts and mortgages were with New York banks except for the mortgage on the Sparta house.

25. The auditor testified that the Sparta residence was a summer home as was demonstrated by the very low telephone bills during the winter months. Also, as indicated on petitioners' check #3265, dated August 16, 1984, written to Sears, it states that Mr. Smith's summer residence is 518 West Shore Trail in Sparta. As of the date when this particular check was written, i.e., August 16, Mr. Smith had a Colorado driver's license as is indicated on the reverse side of the check. However, on check #2494 which was dated April 9, 1983 and written to Sears, Mr. Smith displayed a New York driver's license number. Another indication that the Sparta home was a summer residence was the fact that, although petitioners closed on the

property in December of 1982, their belongings were not shipped from their apartment in Denver to Sparta until April of 1983.

26. For the year 1986, the checks written for the monthly telephone bills for the New Jersey house were for the following amounts:

\$ 4.11 paid on 2/23/86	check #4117
\$ 44.54 paid on 4/21/86	check #4199
\$ 32.04 paid on 5/13/86	check #4238
\$ 52.09 paid on 6/23/86	check #4293
\$ 95.48 paid on 7/15/86	check #4337
\$138.62 paid on 8/19/86	check #4391
\$150.88 paid on 9/14/86	check #4429
\$ 63.41 paid on 10/15/86	check #4465
\$ 40.44 paid on 12/8/86	check #4543
\$ 64.49 paid on 12/22/86	check #4603

27. For the year 1986, the checks written for the monthly telephone bills for the New York City apartment were for the following amounts:

\$ 57.03 paid on 2/1/86	check #4097
\$ 89.11 paid on 3/8/86	check #4141
\$ 54.60 paid on 4/6/86	check #4174
\$ 65.09 paid on 5/13/86	check #4229
\$ 81.46 paid on 6/4/86	check #4271
\$107.84 paid on 7/6/86	check #4317
\$111.54 paid on 8/5/86	check #4364
\$122.84 paid on 9/10/86	check #4414
\$228.97 paid on 10/1/86	check #4447
\$127.20 paid on 11/2/86	check #4494
\$100.74 paid on 12/8/86	check #4546
\$ 88.37 paid on 12/31/86	check #4638

28. For the year 1987, the checks written for the monthly telephone bills for the New Jersey house were for the following amounts:

\$ 16.72 paid on 4/1/87	check #4756
\$ 24.94 paid on 4/22/87	check #4786
\$ 36.82 paid on 5/24/87	check #4848
\$ 41.74 paid on 6/21/87	check #4918
\$ 54.64 paid on 7/21/87	check #4947
\$ 98.73 paid on 8/24/87	check #4996
\$109.49 paid on 9/18/87	check #5041
\$ 41.23 paid on 10/28/87	check #5100
\$ 15.87 paid on 11/14/87	check #5146
\$ 27.19 paid on 12/13/87	check #5215

29. For the year 1987, the checks written for the monthly telephone bills for the New York City apartment were for the following amounts:

\$ 46.50 paid on 2/8/87	check #4698
\$ 72.72 paid on 3/5/87	check #4730
\$ 46.65 paid on 4/1/87	check #4757
\$ 89.23 paid on 5/1/87	check #4810
\$ 66.32 paid on 6/1/87	check #4879
\$114.30 paid on 7/20/87	check #4948
\$115.16 paid on 8/3/87	check #4978
\$ 83.27 paid on 9/2/87	check #5020
\$ 80.75 paid on 10/1/87	check #5057
\$122.04 paid on 11/4/87	check #5127
\$145.56 paid on 12/5/87	check #5171
\$120.01 paid on 12/31/87	check #5261

30. For the year 1988, the checks written for the monthly telephone bills for the New Jersey house were for the following amounts:

\$ 10.09 paid on 2/6/88	check #5307
\$ 36.33 paid on 2/19/88	check #5331
\$ 7.96 paid on 3/12/88	check #5384
\$ 21.36 paid on 4/23/88	check #5437
\$ 22.08 paid on 5/24/88	check #5468
\$ 55.64 paid on 6/13/88	check #5503
\$ 86.81 paid on 7/20/88	check #5560
\$104.51 paid on 8/16/88	check #5605
\$ 90.47 paid on 9/30/88	check #5658
\$126.94 paid on 10/16/88	check #5675
\$ 27.49 paid on 12/1/88	check #5751
\$ 37.31 paid on 12/31/88	check #5827

31. For the year 1988, the checks written for the monthly telephone bills for the New York City apartment were for the following amounts:

\$101.98 paid on 2/6/88	check #5318
\$170.50 paid on 3/1/88	check #5368
\$125.23 paid on 4/8/88	check #5416
\$127.77 paid on 5/6/88	check #5454
\$ 85.66 paid on 6/13/88	check #5510
\$109.79 paid on 7/8/88	check #5541
\$ 68.81 paid on 7/30/88	check #5580
\$ 28.50 paid on 9/1/88	check #5626
\$ 78.57 paid on 10/2/88	check #5670
\$ 99.03 paid on 11/5/88	check #5706
\$106.07 paid on 12/11/88	check #5745
\$120.26 paid on 12/31/88	check #5812

32. For the year 1989, the checks written for the monthly telephone bills for the New Jersey house were for the following amounts:

\$ 25.37 paid on 2/13/89	check #5877
\$ 68.49 paid on 4/8/89	check #5936
\$ 85.52 paid on 4/23/89	check #5962

\$ 7.36 paid on 7/26/89	check #6099
\$ 95.21 paid on 8/20/89	check #6125
\$ 96.98 paid on 10/1/89	check #6186
\$ 11.99 paid on 10/25/89	check #6225
\$ 46.86 paid on 11/16/89	check #6258
\$ 12.00 paid on 12/15/89	check #6345

33. For the year 1989, the checks written for the monthly telephone bills for the New York City apartment were for the following amounts:

\$145.50 paid on 2/13/89	check #5866
\$133.16 paid on 3/12/89	check #5908
\$107.94 paid on 4/8/89	check #5929
\$ 88.66 paid on 5/1/89	check #5986
\$102.05 paid on 6/3/89	check #6022
\$ 96.58 paid on 7/10/89	check #6081
\$ 71.28 paid on 8/20/89	check #6128
\$153.92 paid on 9/1/89	check #6154
\$ 50.62 paid on 10/6/89	check #6205
\$319.77 paid on 11/1/89	check #6236
\$188.31 paid on 12/3/89	check #6282
\$167.41 paid on 12/31/89	check #6365

34. For the year 1990, the checks written for the monthly telephone bills for the New Jersey house were not submitted into evidence.

35. For the year 1990, the checks written for the monthly telephone bills for the New York City apartment were for the following amounts:

\$179.29 paid on 2/1/90	check #6407
\$ 97.30 paid on 3/10/90	check #6465
\$116.37 paid on 4/1/90	check #6494
\$105.92 paid on 5/1/90	check #6536
\$121.42 paid on 6/1/90	check #6569
\$114.75 paid on 7/90	check #6637
\$ 59.48 paid on 8/1/90	check #6669
\$ 77.24 paid on 9/1/90	check #6700
\$159.93 paid on 10/12/90	check #6773
\$159.28 paid on 10/20/90	check #6782
\$140.71 paid on 12/6/90	check #6832
\$133.45 paid on 12/31/90	check #6888

36. For the year 1991, the checks written for the monthly telephone bills for the New Jersey house were for the following amounts:

\$ 13.09 paid on 1/28/91	check #6919
\$ 12.82 paid on 3/1/91	check #6958
\$ 12.82 paid on 4/1/91	check #6996
\$ 14.33 paid on 4/28/91	check #7010
\$ 19.86 paid on 5/23/91	check #7048

\$ 37.34 paid on 6/15/91	check #7079
\$ 44.38 paid on 7/24/91	check #7103
\$109.50 paid on 9/1/91	check #7140
\$ 40.83 paid on 10/18/91	check #7190
\$ 22.00 paid on 12/23/91	check #7268
\$ 37.31 paid on 12/31/91	check #7282

37. For the year 1991, the checks written for the monthly telephone bills for the New York City apartment were for the following amounts:

\$ 94.74 paid on 2/10/91	check #6945
\$127.54 paid on 3/1/91	check #6953
\$108.92 paid on 4/1/91	check #6975
\$136.20 paid on 5/2/91	check #7029
\$191.29 paid on 6/9/91	check #7068
\$167.34 paid on 7/7/91	check #7098
\$ 95.77 paid on 7/31/91	check #7114
\$ 76.22 paid on 9/1/91	check #7141
\$ 78.08 paid on 10/1/91	check #7174
\$107.53 paid on 11/1/91	check #7211
\$130.52 paid on 12/20/91	check #7261

38. Mr. Smith confirmed that there was only one telephone line in the New Jersey home. The phone number was (201) 729-4252. Furthermore, Mr. Smith testified that the 175 East 62nd Street apartment had only one telephone. The phone number was (212) 935-5133.

39. During the years 1986 through 1991, petitioners travelled frequently in their respective businesses. In particular, Ms. Groh testified that she spent a great deal of time in Fairfield, Connecticut working for her major client, the General Electric Company. During these same years, their two young sons (ages five and nine in 1986) attended school in New York City at The Allen-Stevenson School on East 78th Street. According to petitioners' testimony, when the family was staying in Sparta, their daily commute did not necessarily follow the same pattern. For example, when both petitioners worked in New York City, the family, including their nanny, would commute from Sparta to New York City, a distance of approximately 50 miles, with Mr. Smith usually driving. On the days when Mr. Smith was out of town but Ms. Groh was required to go to New York City, she would drive into the City with the boys and the nanny. When neither petitioner was commuting into New York City, one of the drivers from Skidmore would pick up the boys and their nanny and drive them into the City.

Regardless of who drove in the morning, the boys would be dropped off at The Allen-Stevenson School. The family automobile would then be parked at the 62nd Street parking garage. From there, Ms. Groh would usually walk to her office on 57th Street. Mr. Smith would either attend to his business at 175 East 62nd Street or be picked up by one of the Skidmore drivers and be driven to the office on 42nd Street. The nanny would always go to the apartment and either wait for the boys to come home from school or go to the school and get them. During the day she would do secretarial work in connection with petitioners' business projects and investments.

In the evening, according to petitioners, either the family returned in the family automobile or were driven in one of the Skidmore limousines. The Skidmore drivers were also used when Mr. Smith had to go to or return from one of the airports for business travel and when the entire family would be traveling to airports for trips to such places as St. Croix. Mr. Smith testified that either he or the whole family would travel directly from Sparta to the airport on these occasions.

40. Petitioners testified that beginning with the birth of their first child, their nanny, Nellie Gomes, lived with them in Denver, Colorado and later in Sparta, New Jersey. However, the 1987 form W-2 Wage and Tax Statements for both Camille O'Keefe, the daughter of Ms. Gomes, and Nellie Gomes list both of their addresses as 48-16 46th Street, Woodside, New York 11377. Camille O'Keefe took over as nanny in 1988 following the death of her mother. Petitioners testified that Ms. O'Keefe lived with them until 1991, when they determined that a nanny would no longer be required.

41. In an effort to establish the number of days petitioners spent in New York City and State during the years 1986 through 1989, petitioners introduced into the record of this matter eight books, four each for Mr. Smith and Ms. Groh. Each book consists of 12 monthly calendars prepared in anticipation of this hearing. The days of the calendars are marked with locations and numbers. The locations are the places where petitioners claim to have spent that day. Dates left blank on the calendars are deemed to have been spent in New York City. The

numbers indicate the page number of the backup material that follows the calendars. The backup documentation consists of copies of airline tickets, travel vouchers, credit card statements, passports and partnership minutes of Skidmore.

Also introduced was an affidavit from Daniel Friedman with reference to a copy of a portion of Mr. Friedman's business diary for the years 1986 through 1989. Mr. Smith supervised a major construction project for Skidmore in Hartford, Connecticut during 1986 through 1989. The project was known as 180 Allyn Street and was developed by Oakleaf Development Corporation, of which Mr. Friedman was the chairman. The project involved approximately \$265,000,000.00, with Skidmore receiving \$5,000,000.00 in fees. Petitioners also introduced an affidavit from Victoria Kahn who worked with Mr. Smith on a project to bring the Commodities Exchange to Harborside, New Jersey. During the years 1988 through 1990, Mr. Smith would travel to Harborside to work on the project.

42. During the period 1986 through 1990, Ms. Groh testified that she did a great deal of work for the General Electric Company headquartered in Fairfield, Connecticut. An affidavit of Thomas Noonan, head of the Engineering and Construction Operation for RECO (the Real Estate and Construction Operation) of the General Electric Company in Fairfield, Connecticut for the years 1986 through 1994 stated that he observed Ms. Groh approximately two days per week in Fairfield working on projects for the GE Company.

43. Mr. Smith did not submit contemporaneous diaries for the years 1986 and 1987 because they were destroyed in Hurricane Hugo. Mr. Smith did submit diaries for the years 1988 and 1989. Ms. Groh did not submit contemporaneous diaries for the year 1986 and the first ten months of 1987. Diaries were submitted by Ms. Groh for the last two months of 1987 and the years 1988 and 1989.

44. During the year 1986, Mr. Smith claimed to have spent 121 days in New York. There were 46 travel days in which petitioner was either departing from or arriving at a New York airport or railway station. Petitioner claimed 32 days outside of the State but there existed no documentation to support such claim. These days are January 9, 13, 17, 22, 27, 31, February

7, 27, March 6, 7, 31, April 7, 22, May 8, 9, June 4, 16, 27, July 1, 2, 21, 25, 30, August 1, 22, 26, October 24, November 7, 14, 18, December 5 and 10.

A review of purchases made by Mr. Smith for his business operations revealed additional New York City days as follows:

DATE	CALENDAR LOCATION	NYC RECEIPT LOCATION
1/16/86	Hartford	New York City
1/21/86	Hartford	Genovese
3/3/86	Morristown	New York City
3/11/86	Minneapolis/Edmonton	Lexington Hardware
5/30/86	Elizabeth/Sparta	New York City
7/5/86 (weekend)	Sparta	New York City
8/6/86	Chicago	New York City
8/23/86 (weekend)	Sparta	New York City
10/7/86	London	New York City
11/10/86	Hartford	Lamston's
12/7/86 (weekend)	Sparta	Jems Sounds
12/9/86	Hartford	Lamston's
12/14/86 (weekend)	Sparta	Jems Sounds

The monthly calendar contains the following conflicts between the location entered on the calendar and the location of the American Express charge receipts signed by Mr. Smith for that particular day:

DATE	CALENDAR ENTRY	CHARGE LOCATION
2/24/86	Hartford	NYC-AmEx
5/21/86	St. Croix	NYC-AmEx
8/13/86	Sparta	NYC-AmEx

Finally, there existed a receipt indicating that phone products were purchased from AT & T in New York City on December 19, 1996 as reflected by the American Express transaction date recorded therein. The monthly calendar indicated that Mr. Smith was in Hartford on that day.

45. For the year 1987, Mr. Smith stated that he was in New York City for 118 days. A review of documentation submitted for the purpose of substantiating certain business expenses indicated discrepancies between the monthly calendar and the cash register receipts and credit

card information, as follows:

DATE	CALENDAR ENTRY	NYC RECEIPT LOCATION
1/4/87	St. Croix	A & P
1/9/87	Hartford	Bloomingdale's
1/29/87	St. Croix	Gristedes
2/4/87	Hartford	A & P
2/5/87	Boston	NYC
2/12/87	Philadelphia	NYC
2/18/87	Hartford	NYC
2/24/87	Hartford	Gristede's
3/11/87	Hartford	NYC
3/13/87	St. Croix	NYC
3/18/87	St. Croix	NYC
3/27/87	St. Croix	Bloomingdale's
4/4/87	Dayton	NYC
4/15/87	Hartford	Forbidden Planet
5/6/87	Hartford	AmEx transaction
5/10/87	St. Croix/Sparta	NYC
5/15/87	Elizabeth	Gasnick's Supply
5/19/87	Ft. Lee/Elizabeth	A & P
5/23/87 (weekend)	Sparta	Gristede's
6/10/87	Hartford	Pathmark Drugs
6/13/87 (weekend)	Sparta	Lazy Susan
6/25/87	St. Croix	Kentucky Fried Chicken
7/14/87	Hartford	Regents Fabrics
7/17/87	Morristown	NYC
7/31/87	Morristown	Bloomingdale's
8/5/87	Hartford	Gristede's
8/7/87	Elizabeth/Sparta	Taxicab
8/24/87	Chicago	NYC
9/4/87	Chicago	NYC
9/8/87	St. Croix	Gristede's
9/12/87	St. Croix	Jems Sounds
9/14/87	Sparta	A & P
9/17/87	Hartford	Gristede's
9/23/87	Hartford	Sunnyside
9/28/87	Morristown	NYC
9/28/87		Presbyterian Hosp.
10/2/87	Hartford	Lighting Center
10/5/87	Morristown	Gristede's
10/6/87	Boston	NYC
10/14/87	Hartford	Gristede's
10/14/87		The Gap
10/30/87	St. Croix	Bloomingdale's
11/2/87	Hartford	NYC
11/3/87	Hartford	AmEx receipt
11/16/87	Sparta	AmEx receipt
11/21/87	St. Croix	NYC
11/24/87	St. Croix	Gristede's
12/5/87 (weekend)	Sparta	Alexander's
12/16/87	Hartford	Lighting Center
12/19/87	St. Croix	NYC

12/21/87
12/29/87

St. Croix
St. Croix

Gristede's
NYC

Petitioner claimed 23 days outside of the City and State but there existed no documentation for such claim. These days are February 9, March 9, 12, April 8, 28, May 14, 20, June 2, 5, 16, 22, 24, July 3, 6, 7, 15, 23, August 12, 21, 27, September 16 and October 9. All except two of the flights taken by Mr. Smith during 1987 departed from or arrived at either Kennedy or LaGuardia airports. There were 52 such departure and arrival days during the year.

46. For the year 1988, Mr. Smith admitted to being in New York City 136 days during the year. In addition, the following discrepancies existed between certain calendar entries on petitioner's monthly calendars and American Express receipts signed by Mr. Smith:

DATE	CALENDAR ENTRY	NYC AMEX RECEIPT
3/6/88	Aspen	Alo Alo
3/16/88	London	Water Club
5/4/88	Chicago	Spritzer & Fuhrmann
5/31/88	St. Croix	Sichuen Pavillin
6/12/88	Orlando	Sistina
6/15/88	Chicago	NY Helmsley Fiorella Ristorante
7/14/88	Chicago	Bruno
9/15/88	Washington	NY Helmsley/Bruno
9/16/88	Boston	Bruno
11/4/88	San Francisco	Arizona
11/18/88	Chicago	Alo Alo
12/2/88	London	Fortune Garden
12/13/88	Hartford	Willoughby's
12/16/88	Chicago	Agra Restaurant

Of these additional 14 days indicated to be within New York City by the signed American Express receipts, 13 of these days involved charges made either before departing from or after arriving in the City by airplane. Although petitioner consistently testified that it was his pattern to be driven directly to the airport from Sparta or directly to Sparta from the airport, it is obvious that his pattern of travel, as demonstrated by this documentation, was different from what was disclosed by Mr. Smith. There are also 41 additional travel days that were not included as New York City days in Mr. Smith's count analysis.

The following days are listed as non-New York days but do not have any backup documentation to support this claim: January 11, 18, 27, February 1, 22, March 15, 25, 26, 29,

May 6, 23, June 24, July 1, August 22, 26, September 2, 9, October 17, 24, November 1, 16 and December 6.

47. For the year 1989, Mr. Smith indicated that he was in New York 145 days. In addition, the following discrepancies existed between the monthly calendar entries and certain American Express receipts signed by Mr. Smith:

DATE	CALENDAR ENTRY	AMEX RECEIPT-NYC
1/21/89 (weekend)	Sparta	Ranis Electronics
1/25/89	Hartford	Sichuen Pavillion
1/27/89	Chicago	Helmsley Hotel
9/29/89	St. Croix	Agra Restaurant
10/18/89	Toronto	Docks
10/27/89	St. Croix	La Hosteria ¹
10/29/89 (weekend)	St. Croix	Pancho Villa's
12/8/89	Chicago	Agra Restaurant

There existed other receipts which place Mr. Smith in New York City on days he indicated were spent in other locations:

DATE	CALENDAR ENTRY	NYC-RECEIPT
6/3/89 (weekend)	Sparta	Barnes and Noble
10/28/89 (weekend)	St. Croix	Pathmark Drugs
11/26/89 (weekend)	St. Croix	Receipt
11/27/89	Montreal	Lexington Luggage
12/2/89 (weekend)	Sparta	Genovese

There were 34 travel days in which petitioner departed from or arrived at an airport located in New York City. In addition, there were 24 days which petitioner indicated were spent outside of New York but for which no substantiation of the location was provided. The 24 unsubstantiated days were as follows: January 17, 18, 23, 26, 28, February 6, 13, 16, March 9, April 26, May 25, June 23, July 3, 4, 5, 7, August 4, 11, 18, 25, October 11, 24, November 13 and 16.

48. For the year 1986, Ms. Groh indicated that she spent 141 days in New York City

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This receipt appears twice in the documents presented to establish certain business expenses for the year 1989. Mr. Smith indicated on one of the receipts that it represented a dinner with J. Hartman and on the other receipt, he states that it was a dinner with D. Thomas.

during the year. She had 26 travel days where she left from or arrived in New York City in relation to a trip claimed to have been taken outside the State. There were 69 days claimed to have been spent in Fairfield, Connecticut during the year, but no substantiation was offered. Finally, the following 17 days were claimed to have been spent outside New York City but documentation produced by petitioners indicated otherwise:

DATE	CALENDAR ENTRY	NYC-AMEX TRANSACTION
1/18/86 (weekend)	Sparta	Bloomingdale's
5/28/86	Fairfield	Bloomingdale's
		Fortune Garden
6/13/86	Sparta	Bloomingdale's
7/16/86	Fairfield	Bloomingdale's
7/30/86	Fairfield	Bloomingdale's
7/31/86	Fairfield	Bloomingdale's
8/5/86	Fairfield	Bloomingdale's
8/13/86	Fairfield	Doubleday Bookshop
8/14/86	Fairfield	FAO Schwartz
8/26/86	Fairfield	Bloomingdale's
9/12/86	Chicago	Bistro at Trump Tower
10/9/86	Nantucket	Bistro at Trump Tower
11/15/86 (weekend)	Sparta	Maxwell Plum's
		Paragon Athletic Goods
11/19/86	Fairfield	FAO Schwartz
11/22/86 (weekend)	Sparta	The Gap/Alo Alo
11/23/86 (weekend)	Sparta	Chaifteld's Ltd.
		DeMarchelier
12/7/86 (weekend)	Sparta	Lazy Susan

49. Ms. Groh conceded she spent 144 days in New York City during the year 1987. Ms. Groh was also in New York City on the following days as indicated by the American Express receipts from the following locations:

DATE	CALENDAR ENTRY	NYC AMEX RECEIPT
2/8/87 (weekend)	Sparta	Dolphin Seafood
5/6/87	Fairfield	Doubleday Bookshop
6/30/87	West Palm Beach	Bloomingdale's
9/12/87 (weekend)	Sparta	Ralph Lauren
11/11/87	Fairfield	Bloomingdale's
12/5/87 (weekend)	Sparta	Alexander's

Ms. Groh had 28 travel days in which she began and/or ended a trip within the State, and she had 63 calendar entries indicating days spent in Fairfield, CT without any documentation to support such entries.

50. During 1988, Ms. Groh conceded that she spent 137 days in New York City. She claimed to have spent 65 days in Fairfield, CT during the year, but did not submit any receipts which indicated such a presence. In addition, there were 27 travel days which were not counted as New York City days and 3 days for which there existed documentation that indicated the days should have been counted as New York City days. The 3 days are as follows:

DATE	CALENDAR ENTRY	NYC RECEIPT
2/6/88 (weekend)	Sparta	Toy Park
3/4/88	Aspen	Fiorella Restaurant(AmEx)
12/20/88	St. Croix	Sussex Wine

51. During 1989, Ms. Groh conceded that she spent 145 days in New York City. She claimed to have spent 64 days in Fairfield, CT during the year, but did not submit any documentation which indicated such a presence. In addition, there were 37 travel days where Ms. Groh departed from or arrived at a New York City airport which were not counted as New York City days and 3 days for which there existed receipts which indicated the days should have been counted as New York City days. The 3 days are as follows:

DATE	CALENDAR ENTRY	NYC RECEIPT
1/13/89	Orlando	Bistro at Trump Tower(AmEx)
6/5/89	Los Angeles	Nails by Josephine
9/16/89	Sparta	Mulholland Dr Cafe

52. The Division conceded that petitioners spent fewer than 184 days in New York (State and City) during each of the years 1990 and 1991. In the audit report, the auditor indicated that Mr. Smith spent his days during these two years as follows:

	<u>New York</u>	<u>New Jersey</u>	<u>St. Croix</u>	<u>Connecticut</u>	<u>Others</u>
1990	126	69	57	54	59
1991	143	84	38	60	40

Petitioners did not present any information as to their whereabouts during the years 1990 and 1991.

53. During 1986, petitioners paid \$50,355.00 in interest payments to the Union Chelsea National Bank of New York City in connection with a loan for business and investment activities as indicated by customer statements of account and paid \$2,549.00 to the Internal

Revenue Service for interest on a tax liability for an earlier year, for a total of \$52,904.00.

During 1988, petitioners made interest payments in the following amounts: \$27,802.59 to Chase Manhattan Bank of New York City for a loan used to buy out Ms. Groh's partner in GN Associates, \$7,520.68 to Chemical Bank of New York City, \$1,760.20 to Maryland Bank and \$62,261.00 to Citytrust of New York City for loans used in connection with Mr. Smith's business activities in Tarrytown, New York and Denver, Colorado and \$43,200.00 to Pacific Savings Bank for a loan used in connection with petitioners' business activities in an apartment on North Michigan Avenue in Chicago, Illinois as indicated by promissory notes, a letter from Chase Manhattan Bank, records of interest paid and checks written to various banks. Petitioners also made \$42,000.00 in interest payments to the Scotiabank of the Virgin Islands for a construction loan used in connection with petitioners' business activities in St. Croix based upon a letter from the bank and checks written to the bank.

For 1989, petitioners paid \$50,926.00 in interest to Chase Manhattan Bank and \$20,950.00 in interest to Citytrust in connection with their business activities. This is indicated by two records of interest paid from the Chase Manhattan Bank and an interest statement from Citytrust.

All interest discussed herein was claimed by petitioners on their Federal form 1040s, Schedule A, itemized deduction forms.

In 1988, petitioners received \$255,258.00 in interest income, \$2,366.00 in dividend income and \$112,487.00 in capital gain income. For 1989, petitioners received \$211,237.00 in interest income and \$6,061.00 in dividend income.

54. Petitioners claimed passive losses for 1987 through 1991 which were taken on their Federal Schedule E. The losses for 1987, 1990 and 1991 were allowed on audit while the losses for 1988 and 1989 were disallowed. In a telephone conversation with petitioners' representative on November 22, 1994 and in a letter to the representative on November 23, 1994, the auditor indicated that the full amount of the passive losses for 1988 of \$47,782.00 and for 1989 of \$148,104.00 should have been allowed.

55. In addition to their house on St. Croix, petitioners conducted a business which rented the three units that are located on Annas Hope. The rental units were converted from the three buildings that were located on the property at the time petitioners bought Annas Hope in April 1986. The conversion work was done by Caribbean Construction Services & Associates at a cost of \$491,711.00 to petitioners and secured by a mortgage with Scotiabank. Starting in 1987, petitioners included their rental business in St. Croix on a Schedule E - Supplemental Income Schedule with their Federal income tax return, Form 1040. The Schedule E's were audited by New York State for the years 1987 through 1991. For the years 1987, 1990 and 1991, the auditors accepted the documentation produced by petitioners as to the income and expenses shown on the schedules. For the years 1988 and 1989, the auditor disallowed all the expenses listed on the Schedule E's related to petitioners' rental activity on St. Croix. During the course of the hearing, petitioners produced cancelled checks for all of the expenses and Mr. Smith testified that the expenses were necessary in connection with the carrying on of the rental activity in St. Croix during 1988 and 1989.

56. Petitioners claimed certain unreimbursed business expenses on Statements 1 and 2 for the year 1986 and on Statement 1 for the years 1987 through 1991. The unreimbursed business expenses were divided equally between petitioners' Schedules A and E. Petitioners introduced checks written on petitioners' personal checking accounts with New York City banks to support the expenses claimed.

57. As indicated by checks introduced into the record, all Sparta telephone and utility costs were taken as necessary and customary business expenses of the 175 East 62nd Street apartment on petitioners' 1986 Federal income tax return, Statements 1 and 2, and the 1987 Federal income tax return, Statement 1.

58. As indicated by checks introduced into the record, all Sparta telephone and utility costs were taken as necessary and customary business expenses of the 175 East 62nd Street apartment on petitioners' 1988 Federal income tax return, Statement 1 and their 1989 Federal income tax return, Statement 1.

59. As indicated by checks introduced into the record, the Sparta utility expense for the year 1990 was taken as a necessary and customary business expense of the 175 East 62nd Street apartment on petitioners' 1990 Federal income tax return, Statement 1.

60. As indicated by checks introduced into the record, the Sparta telephone expense for the year 1991 was taken as a necessary and customary business expense of the 175 East 62nd Street apartment on petitioners' 1991 Federal income tax return, Statement 1.

61. Mr. Smith testified that there was a television equipped with cable in the children's bedroom. As indicated by checks introduced into the record, petitioners took a full deduction as customary and necessary business expenses all the checks written to Manhattan Cable for years 1986, 1987, 1988, 1989 and 1990.

62. The expenses claimed by petitioners for the year 1986 in their business activities were allocated 10% to Ms. Groh (Statement 1) and 90% to Mr. Smith (Statement 2). The Statement 1 expenses for 1986 begin with a claim for utility expenses of \$185.00. In support, petitioners introduced into evidence copies of checks payable to Jersey Central, which is the utility which supplied electricity to the Sparta house. In support of their claim of \$8,751.00 in office supplies, petitioners introduced a series of checks totalling that amount. The notations on some of the checks indicated that they were written for the St. Croix properties. Petitioners' accountant was questioned at the hearing as to why he treated the unreimbursed business expenses in a manner that allocated them equally between Schedules A and E, and he responded only that that is how he reported the expenses. In addition, with respect to the expenses incurred by Ms. Groh, it was not explained why such expenses were not reported on the corporate tax return of GN Design. Petitioners presented checks totalling \$6,919.00 in support of the amount claimed as labor costs. No explanation was provided as to who received the checks and what their relationship was to petitioners' business activities. Business expenses for subscriptions to magazines and books for the New York office were claimed in the amount of \$2,821.00. Four of the checks submitted and paid to "Kimberly May" totalling \$468.00 were identical to checks submitted as labor costs. The travel expenses of \$5,187.00 and the

entertainment expenses of \$7,669.00 claimed on the return were supported by 3 checks and 18 pages of petitioners' American Express Year-End Summary of Charges for 1986. Twelve checks written to "62nd Street East, Inc." for the monthly maintenance assessment for the New York City apartment totalling \$33,502.00 were introduced to establish the claimed maintenance expense of \$3,350.00. For the telephone expense of \$1,921.00, petitioners submitted 22 checks written to New York Telephone and United Telephone totalling \$1,921.00. Ms. Groh claimed 10% of this total as her expense.

63. Mr. Smith claimed his unreimbursed business expenses on Statement 2 of the 1986 return and allocated them 50% to Schedule A and 50% to Schedule E. Checks and American Express Year-End Summary of Charges for 1986 were submitted in support of the office supplies expense claimed of \$81,087.00. However, 13 of the checks totalling \$1,196.00 were written to "M. Fostnocht & Co.", M. Fostnocht being the woman who cleaned the Sparta house. Checks issued to "Griffith Floors" for \$800.00, "A-1 Peck Office Supplies" for \$852.24 and 4 checks issued to "Larry White Co." totalling \$1,400.00 did not contain the MIRC encoding which appears on the lower right hand corner of a check after it has been processed through the banking system. This encoding signifies that the amount of the check has been paid to the payee of the check. The MIRC encoding is the same number as the amount of the check.

Included in the expense claimed for utilities for the New York City apartment were checks written to New York Telephone of which Mr. Smith deducted 90%, the deduction of 90% of the Sparta utility bills in the amount of \$1,853.00, 100% of the Manhattan Cable expense in the amount of \$203.00 and 100% of the United Telephone of New Jersey bills in the amount of \$686.00.

Insurance expenses in the amount of \$9,279.00, entertainment expenses in the amount of \$15,317.00, maintenance expenses on the New York apartment in the amount of \$30,151.00 and travel expenses in the amount of \$16,932.00 were supported by copies of checks and the year-end summary charges from American Express in the appropriate amounts.

Six checks were submitted in support of the professional expense taken in regard to the

212-214 East 71st Street building in the amount of \$8,017.00. However, one check in the amount of \$2,592.00 was not cashed by any banking institution.

The documentation presented to establish the miscellaneous expenses of \$5,544.00 consisted of cash register receipts which did not identify the item purchased. In addition, the six file cabinets listed on an invoice from Sparta Stationery Plus, Inc. for \$838.52 were previously claimed as an office supply expense. In support of the labor expense in the amount of \$32,015.00, petitioners introduced a series of checks in that amount. However, seven checks totalling \$3,826.00 appeared more than once.

64. On their U.S. Individual Income Tax Return for 1987, petitioners claimed unreimbursed business expenses on Statement 1 and allocated the total 50% to Schedule A and 50% to Schedule E. Petitioners claimed a supplies expense of \$20,285.00 and submitted statements from Skidmore indicating reimbursable and nonreimbursable costs, American Express Year-End Summary Charges for 1987 and charge card statements from Chase Manhattan Bank and Chemical Bank of New York. The reimbursable cost statements from Skidmore totalled \$4,595.00.

Petitioners claimed \$28,666.00 in expenses for office supplies. In support of their claim, they submitted copies of checks with a handwritten notation next to the check as to its purpose. No invoices were submitted. Included among the checks is: one written to the "Postmaster" for the rental fee of the Sparta post office box, several checks with the notation that they are for cleaning services, two checks that are characterized as contributions, two checks written to Sparta Water Co., two checks written for a flag and a flagpole, checks written for window washing, and numerous checks with the notations that they were, for example, for kitchenware, glassware, fabric, bath blinds, towels and a bedroom lamp.

The checks submitted to substantiate the expenses for utilities included checks written to United Telephone of New Jersey, Jersey Central and Service Electric Co. (Sparta electric and utilities), Manhattan Cable, New York Telephone (\$1,152.57) and AT & T (\$359.12 for the purchase of telephones).

Checks addressed to various insurance companies in the amount of \$4,533.00 were submitted in support of the insurance expense taken. However, check #4854 in the amount of \$255.56 was not cashed by any banking institution.

Petitioners submitted checks and mortgage statements for professional fees and mortgage expense in the amounts of \$14,489.00 and \$14,268.00, respectively. Submitted in support of the labor expense was a series of checks totalling \$101,464.00, which was divided into three categories (office, labor, 212 East 77th St.) to arrive at the deducted figure of \$34,821.00. Thirteen of the checks were not MIRC-encoded. The total of these checks was \$1,790.00. Two of the checks that were cashed appear twice within the exhibit.

There are ten checks totalling \$1,284.00 written to Mrs. Fostnocht, the cleaner of the Sparta house. Under cleaning and maintenance, petitioners submitted checks in the amount of \$7,506.00 for the maintenance of the plants in the New York office.

For the entertainment and travel expenses, petitioners submitted checks and credit card statements in the amounts of \$25,293.00 and \$27,171.00, respectively. For the maintenance expenses of \$30,238.00, petitioners submitted checks addressed to "62nd Street East, Inc." and a check for payment of the garage rent totalling the amount claimed.

Invoices and cash register receipts were presented in an effort to support the claimed miscellaneous expenses of \$2,551.00. Many of the cash register receipts did not identify the item purchased. Some of the many items that are listed on the cash register tapes included groceries, dinnerware, greeting cards, candles, party goods, coffee beans, two burgers, an order of french fries and two malts and a dinner at Kentucky Fried Chicken. No explanation was provided as to how these or any of the other items were related to petitioners' business activities. In addition, several of the checks written in payment of the invoices submitted in support of the miscellaneous expenses were previously submitted as office expenses and utility expenses, totalling \$781.21 and \$359.12, respectively. In support of the travel expenses, petitioners introduced computer printouts from Skidmore listing reimbursable expenses.

65. On their U.S. Individual Income Tax Return for 1988, petitioners claimed

unreimbursed business expenses on Statement 1 and allocated the total 50% to Schedule A and 50% to Schedule E. Invoices, cash register receipts and checks were submitted in support of the office supplies expense claimed in the amount of \$29,566.00. Included in the documents submitted are receipts for the purchase of: Armor-all, aluminum foil, Crest toothpaste, Centrum vitamins, Insoles, an item at Kay-Bee Toy Store, a Mars candy bar, greeting cards, the annual post office box rental for the Sparta house, produce, a deli sandwich and a golf computer game. There are also numerous receipts that do not identify the item purchased. There are checks written to American Airlines, GN Associates and the Connecticut Broadcasting Co.

Checks introduced for supplies in the amount of \$44,241.00 include: a check in the amount of \$3,404.12 payable to Buccaneer Bay Landowners Association, check #5559 payable to Morgan-Francis Co. which is the company that sold the flagpole to petitioners for the St. Croix property, check #5295 to Fisher Skylights which is the company that petitioners contracted to do the lighting on their St. Croix house, check #1285 in the amount of \$5,000.00 written to K. Robert Najarian who was Ms. Groh's partner at GN Associates, four checks written to A. Lasley or Allison Lasley totalling \$5,238.61 and two checks totalling \$2,300.00 payable to A & S Landscaping. No explanation was provided as to how these checks related to supplies for petitioners' business activities.

Checks presented in support of the utility expenses in the amount of \$8,224.00 included: a check in the amount of \$1,298.00 payable to E. A. Lugo Co., the company which provided the audio-visual equipment for the St. Croix residence, twelve checks totalling \$1,533.47 written to Jersey Central for the monthly utilities of the Sparta house, twelve checks written to the United Telephone Co. in the amount of \$626.99, eleven checks written to Manhattan Cable totalling \$341.97 and twelve checks written to Madelyn Simon totalling \$3,045.34. One of the checks indicated that these were for maintenance.

Petitioners submitted checks totalling \$16,158.00 in regard to the insurance expense claimed. The checks contained five different insurance companies: State Farm, USAA, Chubb, Marshall & Sterling and Mutual Insurance Company of New York. Marshall & Sterling was

the insurance company that issued the policy for the St. Croix property. State Farm was the insurance company that issued the policies for the Sparta home and the 1986 Chevrolet Blazer. There was no testimony concerning what the other three insurance companies insured.

Petitioners submitted checks equal to the amount of the expenses claimed for professional fees and payroll and other taxes totalling \$95,616.00 and \$3,500.00, respectively. Petitioners submitted checks totalling \$104,668.00 with regard to their claimed labor expense. However, check #5243 in the amount of \$1,298.80 was also presented in support of the utility expense; checks #1205, #1208, #1155, #1285, #1224, #1240, #1174, #1167, #1171, #5561 and #5732 totalling \$14,238.43 were also presented in support of supplies expense; and, checks #1164, #1156 and #1165 totalling \$2,773.60 were also presented in support of the office supply expenses. In addition, nine checks totalling \$1,155.00 were written to the Sparta housekeeper, Mrs. Fostnocht. No testimony was offered explaining who many of the payees named on the checks were and what services they performed for petitioners.

66. On their U.S. Individual Income Tax Return for 1989, petitioners claimed unreimbursed business expenses on Statement 1 and allocated the total 50% to Schedule A and 50% to Schedule E. Included in the checks submitted in support of the labor expenses in the amount of \$67,809.00 were five checks written to the Sparta housekeeper totalling \$440.00 and 32 checks written to Camille O'Keefe, who provided child care services, totalling \$35,700.00. In addition, check #6061 in the amount of \$150.00 and check #6322 in the amount of \$750.00 were not MIRC encoded and thus not cashed by any banking institution.

Year-end summary statements for various credit cards, checks and invoices were submitted to document the claimed business expenses in the amount of \$35,213.00. Included in the checks introduced in support of the \$3,071.00 in telephone expenses were two checks payable to the order of "Ship and Shore Power Systems" totalling \$995.00. On the memo portion of one of the checks, it is noted that the payment is for a deposit on a generator. In addition, there were nine checks totalling \$449.84 payable to United of New Jersey, the telephone company that provided service to the Sparta house. Petitioners claimed utility

expenses in the amount of \$2,562.00 and submitted checks totalling that amount. However, 12 checks were written to Jersey Central and 3 to Sparta Utility. These checks totalled \$1,774.85. There also was included 12 checks payable to Manhattan Cable totalling \$401.17.

Petitioners claimed and submitted checks in the amount of \$3,983.00 for publications and supplies expenses. Petitioners claimed and submitted checks for maintenance and repair expenses in the amount of \$13,505.00 and professional fees in the amount of \$11,932.00.

Petitioners claimed \$40,828.00 in transportation expenses and introduced checks, Skidmore expense statements, year-end credit card statements and credit card receipts in support of their claim. Three checks written to reimburse Skidmore for the amounts on the expense statements were not MIRC encoded and therefore not cashed by any banking institution. The travel expenses covered by these checks totalled \$9,097.00. In addition, a fourth Skidmore expense statement shows travel expenses of \$1,395.40. Meals and entertainment expenses in the amount of \$22,491.49 ($\$28,114.37 \times .80$) were supported by adding machine tapes totalling \$24,926.01, a Skidmore expense statement showing expenses of \$1,798.08 and an uncashed check and checks in the amount of \$1,390.28.

In support of office supply expenses in the amount of \$15,711.00, petitioners submitted checks, credit card summary statements, Skidmore expense statements with accompanying checks written to Skidmore, invoices and credit card statements. None of the checks which accompanied the Skidmore expense statements were cashed by a banking institution. The expenses claimed to be through Skidmore totalled \$5,122.80. An additional four checks, totalling \$2,834.84, were also not cashed by a banking institution.

General supplies expenses in the amount of \$11,026.00 were supported by checks, invoices and cash register receipts. Miscellaneous expenses were claimed in the amount of \$1,594.00 and checks in that amount were submitted. One of the checks was written to the Lake Mohawk Club in the amount of \$575.00. No testimony was offered as to why this would qualify as a business expense for petitioners' real estate ventures. Petitioners claimed and submitted checks in the amount of \$2,166.00 for payroll taxes paid. Advertising expenses were

claimed in the amount of \$950.00 and checks were presented in that amount. The memo on one check indicated it was written for "pillowcovers-cases/kware" while another check was written to Woolworth and two more were written to Bloomingdales. These four checks totalled \$360.00.

67. On their U.S. Individual Income Tax Return for 1990, petitioners claimed unreimbursed business expenses on Statement 1 and allocated the total 50% to Schedule A and 50% to Schedule E. Checks and other documentation were presented in support of the expenses claimed for maintenance of \$45,357.00, publications and supplies of \$1,739.00, miscellaneous of \$666.00, professional fees of \$23,559.00 and meals and entertainment of \$5,774.00. Labor expenses of \$40,913.00 were claimed and supported by checks in the same amount. Three checks totalling \$440.00 were issued to the Sparta housekeeper, Mrs. Fostnocht, and twelve checks totalling \$18,500.00 were written to the children's nanny, Camille O'Keefe.

Checks in the amount of the business expenses claimed were submitted, although one check in the amount of \$250.00 was not cashed by any banking institution as it was not MIRC encoded. Of the checks submitted in respect of the telephone expenses claimed of \$2,603.00, eleven were addressed to Jersey Central totalling \$1,138.00. All the checks introduced as support for the utility expense of \$883.00 were written to Manhattan Cable, George and Diane Zinkken or Robert Parry. These three individuals were not identified in the testimony of petitioners.

Included in the checks submitted for the claimed insurance expense of \$3,578.00 were checks written to State Farm, Chubbs Insurance and Carl Stecker & Associates. No explanation was provided as to what these various insurance companies insured. The claimed transportation expenses of \$16,548.00 were supported by checks, credit card statements, Skidmore expense statements, credit card receipts and travel agency statements. One check in the amount of \$465.00 was not cashed by a banking institution.

68. On their U.S. Individual Income Tax Return for 1991, petitioners claimed unreimbursed business expenses on Statement 1 and allocated the total 50% to Schedule A and

50% to Schedule E. Checks and other documentation were presented in support of the expenses claimed for maintenance of \$46,524.00, publications and supplies of \$957.00 and plants and plant maintenance of \$3,594.00. Federal miscellaneous income tax statements, forms 1099, for the year 1991 and checks were provided in support of the labor expense claimed of \$23,960.00. The total of the checks and the amount shown on the form 1099 in relation to Camille O'Keefe, the nanny of petitioners' children, was \$23,960.00.

Included in the documents submitted relating to the telephone expense claimed of \$1,678.00 were eleven checks written to United Telephone of New Jersey totalling \$364.00. Included in the checks submitted for the claimed insurance expense of \$2,023.00 were checks written to State Farm and USAA. No explanation was provided as to what these insurance companies insured. Three of the checks submitted in support of the claimed professional fees of \$32,846.00 had not been cashed by a banking institution. The three checks totalled \$9,566.00. Documentation submitted on behalf of petitioners in support of the transportation expenses claimed of \$15,294.00 included checks in the amount of \$4,239.00, adding machine tapes totalling \$10,140.00 and hand-written notations with a total of \$915.00. The only documentation submitted in support of the meals and entertainment of \$4,286.00 were adding machine tapes. Included in the checks for the cleaning expense taken of \$5,146.00 were six checks totalling \$760.00 written to the Sparta housecleaner. Among the checks submitted with regard to the repairs expense of \$4,929.00 was a check written to Sparta Electric in the amount of \$431.62. Documentation submitted to substantiate the office supplies of \$9,028.00 were adding machine tapes totalling \$2,286.00 and invoices in the amount of \$6,742.00.

69. Mr. Smith was involved in the purchase and conversion of an apartment building located at 212-214 East 77th Street in New York City. Mr. Smith paid Jon Siegel Real Estate Management Co., Inc. fees in the amount of \$65,500.00 to manage the apartment building in 1986, as indicated by 18 checks written by Mr. Smith to Jon Siegel Management in 1986. These were ordinary and necessary fees in the operation of the apartment building. Petitioners claimed fees of \$69,835.00 on their 1986 Federal Schedule E form.

The cooperative offering plan to convert to cooperative ownership the premises located at 212-214 East 77th Street, New York, New York was declared effective in 1984. At the time of the conversion, the cooperative corporation had a total of 1,340 shares, all owned by Mr. Smith. The total basis for those shares was claimed by petitioners to be \$1,912,546.00, as indicated by the prospectus for conversion, which resulted in a claimed cost per share at the time of conversion of \$1,427.27 ($\$1,912,546.00 / 1,340$). Petitioner Smith sold 492 shares in 1984 and 1985, but none in 1986.

In 1987, Mr. Smith sold the remaining 848 shares in the cooperative corporation to Jon Siegel for a net total of \$623,267.00. On May 18, 1984, petitioners signed a legal instrument, a deed transferring 212-214 East 77th Street, New York, NY, on which their residence was listed as 175 East 62nd Street. As Mr. Smith claimed to have made \$78,541.00 in improvements in the building after its purchase, the sale resulted in a loss of \$665,598.00 ($\$1,210,324.00$ [original basis of \$1,427.27 per share X 848 shares] + \$78,541.00 in improvements = \$1,288,865.00 - \$623,267.00). Subtracting the recaptured depreciation of \$185,675.00 from the loss resulting from the sale of the shares results in a total loss of \$479,923.00 on the sale of the shares of the cooperative corporation of the premises located at 212-214 East 77th Street. Petitioners claimed a loss on the sale of the 848 shares relating to the premises located at 212-214 East 77th Street in the amount of \$506,349.00 on their Federal Form 4797, Gains and Losses From Sales or Exchanges of Assets Used in a Trade or Business and Inventory Conversions, filed with their 1987 returns.

At the hearing, petitioners submitted into evidence the closing statement at the time of conversion in 1984, the prospectus for conversion and the closing statement at the time of sale in 1987. The original closing statement at the time of purchase in 1981 was marked as an exhibit but was not offered into evidence. In addition, the auditor testified that she did not see the closing statement for petitioners' purchase of this property and such information was needed in order to determine a basis in the property.

70. On September 19, 1989, the island of St. Croix sustained a hurricane with winds in

excess of 200 miles per hour. Hurricane Hugo devastated most of St. Croix including Annas Hope. In landscaping alone, petitioners lost 150 palm and other trees, plants and shrubs. Salt water entered the engine of petitioners' water truck, destroying the truck. The fence around the property was blown down, the winds broke the glass windows and doors of their home and rental units, and the ocean waters entered the home and rental units. The winds and water destroyed much of the furniture and the records relating to Mr. Smith's real estate activities which had been transferred to the office in the house on St. Croix from the New York City office.

Repairs to the property were done by Caribbean Construction Services & Associates, the company which had originally been involved in the construction of Annas Hope. The company estimated the cost of the damage done by the hurricane to the rental units and the landscaping to be \$1,021,600.00, to the petitioners' residence to be \$1,206,550.00 and to the loss of rents and use to be \$2,228,150.00. The actual cost of the repairs to the house was \$945,750.00 and the actual cost of the repairs to the rental units was \$798,839.00, as indicated by the repair invoices of Caribbean Construction Services & Associates. Dorchester Insurance Company reimbursed petitioners \$765,000.00 for the losses sustained by petitioners' house and Cigna Insurance Company reimbursed petitioners \$353,598.00 for the losses sustained by the rental units, as established by correspondence and checks from the insurance companies. This resulted in petitioners' sustaining a net loss of \$180,750.00 to their house and a loss of \$445,241.00 to the rental units. It is noted that the insurance coverage maintained by petitioners did not cover the loss to the landscaping, trees or plants.

Petitioners filed a casualty loss claim with their Federal Form 1040 for 1989, accompanied by a Federal Form 4684 - Casualties and Thefts. They did not file a separate form 4684 for each item claimed as a loss in Hurricane Hugo but instead included the total cost of the repairs for the damaged property and the amounts received as insurance reimbursement on the one form 4684. Petitioners used the actual cost of the repairs to the house and rental units as their cost or other basis in completing the form, resulting in casualty losses of \$180,750.00 to

the house and \$445,241.00 to the rental units. On audit, the entire casualty loss was denied.

71. Petitioners filed their Federal US Individual Income Tax Returns, Forms 1040, for the years 1979, 1980 and 1981 from Denver, Colorado, for the years 1982, 1983 and 1984 from Sparta, New Jersey and the years 1985 through 1991 from St. Croix, Virgin Islands. Between 1985 and 1991, petitioners did not file resident tax returns in any of the 50 states. Any state return filed during those years was filed as a nonresident of such state.

Petitioners filed state tax returns as residents in the following jurisdictions: Colorado: 1976-1981; New Jersey: 1982-1984 and a part-year in 1985. Petitioners did not file tax returns with the State of New Jersey for tax years 1986, 1987, 1990 and 1991. While petitioners did file returns for tax years 1988 and 1989, such returns reflected no income.

72. Petitioners filed 1986 and 1987 New York State nonresident income tax returns on July 13, 1987 and June 1, 1988, respectively. On the 1986 return they claimed charitable contributions in the amounts of \$13,320.00 to The Allen-Stevenson School and \$8,921.00 to the Christ Church. On the 1987 return they claimed charitable contributions in the amounts of \$10,020.00 to The Allen-Stevenson School and \$2,760.00 to the Christ Church.

In support of the 1986 Allen-Stevenson School contribution, petitioners submitted seven checks which were written to the school. However, only three of the checks had been cashed, and one of the cashed checks, in the amount of \$7,630.00 and dated August 5, 1986, was a tuition check as testified to by Mr. Smith. The remaining two checks totalled \$2,540.55. Petitioners also presented copies of three letters from The Allen-Stevenson School to petitioners thanking them for their gifts of \$500.00 to the Tuition Raffle, \$2,500.00 to the Annual Fund and \$10,000.00 for the Campaign for Continuing Excellence. The letter relating to the Annual Fund gift in the amount of \$2,500.00 concerns the check in the same amount. A publication put out by The Allen-Stevenson School also indicates petitioners' donation of \$2,500.00. For the year 1987, petitioners submitted three checks totalling \$8,500.00 in support of their charitable contribution deduction to the Stevenson School. Mr. Smith testified that two of the checks totalling \$6,000.00 were "just given to Allen Stevenson". The remaining check in the amount

of \$2,500.00 was paid to the annual fund drive.

No documentation was presented concerning the claimed contributions to the Christ Church.

73. On October 19, 1990, petitioners executed a Consent Extending Period of Limitation for Assessment of Personal Income Taxes Under Articles 22 and 30 of the Tax Law. The consent extended the period of limitation for the period January 1, 1986 through December 31, 1986 to April 15, 1991.

On May 2, 1992, January 14, 1993 and December 29, 1993, petitioners executed three consents extending period of limitation for assessment of personal income taxes under Articles 22 and 30 of the Tax Law. The consents extended the period of limitation for the period January 1, 1988 through December 31, 1988 to April 15, 1995.

On January 14, 1993 and December 23, 1993, petitioners executed two consents extending period of limitation for assessment of personal income taxes under Articles 22 and 30 of the Tax Law. The consents extended the period of limitation for the period January 1, 1989 through December 31, 1989 to April 15, 1993.

On May 25, 1994, petitioners executed a consent extending period of limitation for assessment of personal income taxes under Articles 22 and 30 of the Tax Law. The consent extended the period of limitation for the period January 1, 1990 through December 31, 1990 to April 15, 1995.

74. On July 31, 1990, the Division of Taxation ("Division") issued to petitioners a Statement of Personal Income Tax Audit Changes for the year 1986 asserting additional New York State and City personal income tax due in the amount of \$108,763.41 and \$37,992.55, respectively, plus interest and penalty (Tax Law § 685[b], [p]). The statement indicated that petitioners had been determined to be domiciliaries of New York State and City and that the following claimed expenses had been disallowed: unreimbursed employee business expenses incurred by Ms. Groh in maintaining an apartment in New York City in the amount of \$35,074.00; Schedule A miscellaneous expenses incurred by Mr. Smith in the amount of

\$151,259.00; Schedule A interest expenses paid to the Union Chelsea National Bank and the Internal Revenue Service ("IRS") in the amount of \$52,904.00; charitable contributions made to The Allen-Stevenson School in the amount of \$13,320.00; Schedule E miscellaneous expenses in the amount of \$69,835.00; and partnership expenses incurred to maintain an office in the amount of \$151,259.00, for a total amount disallowed of \$473,651.00.

On the same date, the Division issued a Statement of Personal Income Tax Audit Changes for the year 1987 asserting additional New York State and City personal income tax due in the amount of \$199,709.67 and \$86,052.31, respectively, plus interest and penalty (Tax Law § 685[b], [p]). The statement indicated that petitioners had been determined to be domiciliaries of New York State and City and that the following items had been disallowed: Schedule A office expenses in the amount of \$157,524.00; the claimed loss incurred upon the sale of the 848 shares in the cooperative corporation located at 212-214 East 77th Street in the amount of \$506,349.00; business expenses allocated to partnership income in the amount of \$174,434.00; and Schedule E travel expenses related to the cooperative corporation at 212-214 East 77th Street in the amount of \$11,087.00, for a total amount disallowed of \$849,394.00.

75. On February 15, 1991, the Division issued to petitioners a Notice of Deficiency asserting New York State and City personal income tax due in the amount of \$432,517.95, plus interest and penalty, for the years 1986 and 1987.

76. On June 10, 1994, the Division issued to petitioners a Statement of Personal Income Tax Audit Changes for the year 1988 indicating additional New York State and City personal income tax due of \$105,215.58 and \$44,253.77, respectively, plus interest and penalty (Tax Law § 685[b], [p]). The statement indicated that petitioners had been determined to be domiciliaries of New York State and City. In addition, the statement indicated that itemized deductions had been disallowed in the amount of \$413,929.00, consisting of miscellaneous itemized deductions of \$216,863.00, charitable contributions of \$56,522.00 and investment interest expense of \$140,514.00, and Schedule E income had been increased by \$449,209.00 as the result of the disallowance of certain passive losses.

On the same date, the Division sent a Statement of Personal Income Tax Audit Changes for the year 1989 indicating additional New York State and City personal income tax of \$112,619.93 and \$48,604.99, respectively, plus interest and penalty (Tax Law § 685[b], [p]). The statement noted that petitioners had been determined to be domiciliaries of New York State and City. In addition, the statement indicated that Schedule E income had been increased by \$431,787.00, business casualty losses in the amount of \$445,241.00 had been disallowed in full and \$423,026.00 in itemized deductions had been disallowed as follows: miscellaneous itemized deductions of \$218,185.00, charitable contributions of \$22,673.00, investment interest expense of \$71,990.00 and personal casualty losses of \$110,178.00.

77. On October 13, 1994, the Division issued to petitioners a Notice of Deficiency asserting additional New York State and City personal income tax due in the amount of \$296,659.27, plus interest and penalty, for the years 1988 and 1989.

78. On July 27, 1994, the Division issued to petitioners a Statement of Personal Income Tax Audit Changes for the year 1990 asserting additional New York State and City personal income tax due of \$68,661.68 and \$42,606.91, respectively, plus interest and penalty (Tax Law § 685[b], [p]). The statement noted that petitioners had been determined to be domiciliaries of New York State and City. In addition, the statement indicated that unreimbursed business expenses claimed on petitioners' Schedules A and E had been disallowed in the amounts of \$109,074.00 and \$130,864.00, respectively.

On the same date, the Division sent a Statement of Personal Income Tax Audit Changes for the year 1991 indicating additional New York State and City personal income tax due of \$34,839.49 and \$27,170.51, respectively, plus interest and penalty (Tax Law § 685[b], [p]). The statement noted that petitioners had been determined to be domiciliaries of New York State and City. In addition, the statement indicated that unreimbursed business expenses claimed on petitioners' Schedules A and E had been disallowed in the amounts of \$118,110.00 and \$128,563.00, respectively, and a claimed casualty loss in the amount of \$12,961.00 had been disallowed in full.

79. On October 13, 1994, the Division issued to petitioners a Notice of Deficiency asserting New York State and City personal income tax due in the amount of \$173,278.59, plus interest and penalty, for the years 1990 and 1991.

CONCLUSIONS OF LAW

A. It has been held that "residence" means living in a particular locality but domicile means living in that locality with the intent to make it a fixed and permanent home. To acquire a new domicile there must be a union of residence and intention, animus et factus, either without the other being insufficient. (See, In re Newcomb's Estate, 192 NY 238.)

B. Tax Law § 605(b) provides, in pertinent part, as follows:

"(1) Resident individual. A resident individual means an individual:

"(A) who is domiciled in this state, unless (i) he maintains no permanent place of abode in this state, maintains a permanent place of abode elsewhere, and spends in the aggregate not more than thirty days of the taxable year in this state, or . . .

"(B) who is not domiciled in this state but maintains a permanent place of abode in this state and spends in the aggregate more than one hundred eighty-three days of the taxable year in this state, unless such individual is in active service in the armed forces of the United States."

C. While there is no definition of "domicile" in the Tax Law the Division's regulations (20 NYCRR former 102.2[d]) provided, in pertinent part:

"(d) Domicile. (1) Domicile, in general, is the place which an individual intends to be his permanent home -- the place to which he intends to return whenever he may be absent.

"(2) A domicile once established continues until the person in question moves to a new location with the bona fide intention of making his fixed and permanent home there. No change of domicile results from a removal to a new location if the intention is to remain there only for a limited time; this rule applies even though the individual may have sold or disposed of his former home. The burden is upon any person asserting a change of domicile to show that the necessary intention existed. In determining an individual's intention in this regard, his declarations will be given due weight, but they will not be conclusive if they are contradicted by his conduct. The fact that a person registers and votes in one place is important but not necessarily conclusive, especially if the facts indicate that he did this merely to escape taxation in some other place.

"(3) Domicile is not dependent on citizenship; that is, an immigrant who has permanently established his home in New York State is domiciled here regardless of whether he has become a United States citizen or has applied for citizenship. However, a United States citizen will not ordinarily be deemed to have changed his

domicile by going to a foreign country unless it is clearly shown that he intends to remain there permanently

"(4) A person can have only one domicile. If he has two or more homes, his domicile is the one which he regards and uses as his permanent home. In determining his intentions in this matter, the length of time customarily spent at each location is important but not necessarily conclusive. As pointed out in subdivision (a) of this section, a person who maintains a permanent place of abode in New York State and spends more than 183 days of the taxable year in New York State is taxable as a resident even though he may be domiciled elsewhere."

Permanent place of abode is defined in the regulations at 20 NYCRR former 102.2(e)(1)

as:

"a dwelling place permanently maintained by the taxpayer, whether or not owned by him, and will generally include a dwelling place owned or leased by his or her spouse."

D. To effect a change in domicile, there must be an actual change in residence, coupled with an intent to abandon the former domicile and to acquire another (Aetna National Bank v. Kramer, 142 App Div 444, 126 NYS 970). Both the requisite intent as well as the actual residence at the new location must be present (Matter of Minsky v. Tully, 78 AD2d 955, 433 NYS2d 276). The concept of intent was addressed by the Court of Appeals in Matter of Newcomb (192 NY 238, 250-251):

"Residence means living in a particular locality, but domicile means living in that locality with intent to make it a fixed and permanent home. Residence simply requires bodily presence as an inhabitant in a given place, while domicile requires bodily presence in that place and also an intention to make it one's domicile.

"The existing domicile, whether of origin or selection, continues until a new one is acquired and the burden of proof rests upon the party who alleges a change. The question is one of fact rather than law, and it frequently depends upon a variety of circumstances, which differ as widely as the peculiarities of individuals In order to acquire a new domicile there must be a union of residence and intention. Residence without intention, or intention without residence, is of no avail. Mere change of residence although continued for a long time, does not effect a change of domicile, while a change of residence even for a short time, with the intention in good faith to change the domicile, has that effect Residence is necessary, for there can be no domicile without it, and important as evidence, for it bears strongly upon intention, but not controlling, for unless combined with intention, it cannot effect a change of domicile There must be a present, definite and honest purpose to give up the old and take up the new place as the domicile of the person whose status is under consideration [E]very human being may select and make his own domicile, but the selection must be followed by proper action. Motives are immaterial, except as they indicate intention. A change of domicile may be made through caprice, whim or fancy, for business, health or pleasure, to secure a change of climate, or a change of laws, or for any reason whatever,

provided there is an absolute and fixed intention to abandon one and acquire another and the acts of the person affected confirm the intention No pretense or deception can be practiced, for the intention must be honest, the action genuine and the evidence to establish both, clear and convincing. The animus manendi must be actual with no animus revertendi. . . .

"This discussion shows what an important and essential bearing intention has upon domicile. It is always a distinct and material fact to be established. Intention may be proved by acts and by declarations connected with acts, but it is not thus limited when it relates to mental attitude or to a subject governed by choice."

E. The test of intent with respect to a purported new domicile has been stated as "whether the place of habitation is the permanent home of a person, with the range of sentiment, feeling and permanent association with it" (Matter of Bodfish v. Gallman, 50 AD2d 457, 378 NYS2d 138, 140). Moves to other states in which permanent residences are established do not necessarily provide clear and convincing evidence of an intent to change one's domicile (Matter of Zinn v. Tully, 54 NY2d 713, 442 NYS2d 990). The Court of Appeals articulated the importance of establishing intent, when, in Matter of Newcomb (supra at 251) it stated, "No pretense or deception can be practiced, for the intention must be honest, the action genuine and the evidence to establish both clear and convincing." Performance declarations are less persuasive than informal acts which demonstrate an individual's "general habit of life" (see, Matter of Silverman, Tax Appeals Tribunal, June 8, 1989, citing Matter of Trowbridge, 266 NY 283, 289). A taxpayer may change his or her domicile without "severing all ties with New York State" (see, e.g., Matter of Sutton, Tax Appeals Tribunal, October 11, 1990). The question is whether petitioners' overall conduct contradicted their formal declarations of a change of domicile to Denver, Colorado, Sparta, New Jersey and St. Croix, Virgin Islands.

F. As is evident from the cases cited above, in determining an individual's domicile, the facts and circumstances of the case are paramount. As stated in Matter of Silverman (supra), while certain declarations may evidence a change of domicile, such declarations are less persuasive than informal acts which demonstrate an individual's "general habit of life." A physical move to another place in which a permanent residence is established does not necessarily provide the clear and convincing evidence of an intent to change one's domicile (Matter of Zinn v. Tully, supra). Only when coupled with the clear intent to change one's

domicile does the fact of a changed residence become a true changed domicile.

G. As previously discussed, the question of intent is paramount to the determination of where one has established his or her domicile or whether an individual has changed his or her domicile to another jurisdiction. Initially, through their testimony, petitioners alleged that they were domiciled in New York until 1974, moved to Colorado where they lived until 1982, moved to New Jersey and lived there from 1982 through 1985 and in 1985 moved to St. Croix through the end of the audit period. Petitioners' brief, however, outlined a slightly different schedule of domicile changes. The brief claimed a move from New York to Colorado in 1972, a change to New Jersey in 1983 followed by a move to St. Croix in 1987. In the audit questionnaire that petitioners personally prepared, signed and submitted, petitioners stated that they never stayed in New York during the audit years. This assertion is in direct conflict with their testimony as presented at the hearing. Furthermore, petitioners stated in the audit questionnaire that they first occupied their dwelling at Annas Hope, St. Croix in 1985. This statement is clearly untrue as they did not purchase this property until April 1986 and the house built upon the property was not completed until November 1987. These statements on the part of petitioners not only impair their testimony in general but exhibit a willingness to adjust their "intent" as to their domicile to fit the particular theory being offered. It is again noted that their declarations of intent are less persuasive than the informal acts which demonstrate their "general habit of life".

H. In support of their asserted change of domicile to Denver, Colorado, petitioners put forth testimony but little documentation. There is some documentation in the record, however, that tends to cast a shadow over their testimony. Furthermore, the weight of the testimony offered by petitioners is so impaired by the contemporaneous legal and certified documents in the record that their testimony as to the issue of their move to Denver is entitled to little or no weight.

Petitioners claimed that they neither owned, rented nor maintained a place of abode in New York during the time when they were in Denver between 1972 through 1983. However,

the record is clear that they not only maintained residences in New York City during the period that they claimed to have been in Denver, but that there was never a time after they first moved to New York City in the 1960s that petitioners did not own or rent real property in New York City. Mr. Smith purchased and resided at 211 East 62nd Street in the fall of 1964. He sold this property in March 1977. Petitioners' certified marriage license in 1976 and the certified birth certificate of their first son in 1977 listed their residence as 252 East 51st Street, New York, New York. In January 1978, petitioners had already owned and had telephone service installed at 175 East 62nd Street, New York, New York. The certified birth certificate of their second son listed their residence in 1981 as 175 East 62nd Street, New York, New York. This apartment was owned and maintained by petitioners throughout the audit period.

The record contravenes petitioners' testimony that they did not maintain a permanent place of abode in New York City during the period they claim to have been in Denver, as it has been established that they either owned or rented a place of residence in New York City from 1964 through the audit period. It is interesting to note that the certified documents which contain the information that contrasts with petitioners' testimony are legal documents with information about their residences which was undoubtedly supplied by petitioners. These documents directly contradict the testimony of petitioners and diminish the weight to be given such testimony.

The certified copy of their marriage license stated that petitioners resided at 251 East 51st Street in the Borough of Manhattan and State of New York. The certified birth certificate of their first son stated that on July 15, 1977, the "Mother's Usual Residence" was at 251 East 51st Street, City of New York, County of New York and State of New York. The document further stated that, pursuant to the Bureau of Vital Records, Department of Health, City of New York, the mailing address of the mother was "Mrs. Carol Smith, 251 East 51st Street, Apt. 20-M, New York, New York 10022." The certified birth certificate of their second son stated that on August 18, 1981, the "Mother's Usual Residence" was at 175 East 62nd Street, City of New York, County of New York and State of New York. The birth certificate further provided that

pursuant to the Bureau of Vital Records, Department of Health, City of New York, the mailing address of the mother was "Mrs. Carol Smith, 175 East 62nd Street, New York, New York 10021." Finally, the deed to the Sparta residence listed petitioners' address as 175 East 62nd Street.

As to the topic of their marriage, petitioners testified that they were not married in New York, but rather, were married on the high seas, outside of the jurisdiction of New York State. A review of the certified copy of their marriage license revealed that they were, in fact, married in Yonkers, New York. Thus, petitioners were again less than candid in their testimony, this time concerning the location of their marriage in 1976.

Finally, although initially claiming domicile in Colorado beginning in 1974 through 1981, and later in 1972 through 1982, they filed no returns in Colorado for the years 1974 and 1975.

Under these circumstances, it cannot be found that petitioners exercised a change of domicile to Denver, Colorado during the years 1972 through 1982.

I. Petitioners claimed to have changed their domicile to New Jersey in 1983. As with the earlier attempt to prove that they changed their domicile to Denver, petitioners' testimony is severely impaired by documentation in the record which undermined many of the claims that they made. Initially it is noted that despite the claim of domicile in New Jersey beginning in 1983, which would be consistent with the purchase of the Sparta house in December 1982 and the moving of the furniture into the house in April 1983, petitioners, without explanation, filed as New Jersey residents for the year 1982. Petitioners had their New Jersey telephone bills, New Jersey real property tax bills and Lake Mohawk Country Club statements sent to the New York apartment. A review of the monthly telephone bills for the New Jersey house indicated that usage was minimal during the winter months and increased during the warmer months, which suggested that the house was used on a seasonal basis rather than year round. This conclusion is supported by petitioners having written on checks imprinted with their New York City address that their New Jersey address was a "summer residence". In addition, petitioners' children attended school in New York City during all of the audit years, and the records of The

Allen-Stevenson School listed the childrens' home address as 175 East 62nd Street, New York, New York. Finally, all of the pictures presented of the Sparta house during the summer months were taken in the 1980s while those taken in the wintertime were dated 1992, three years after the commencement of the initial audit. It is also important to note that, although the Sparta house was purchased in December 1982, furniture was not moved into the house until April 1983, again indicating spring and summer month usage of the Sparta house.

J. Initially, petitioners had claimed a change of domicile to St. Croix in 1985, but revised that claim in their brief to November 1987. Inconsistent statements were made during the course of the hearing as they related to the original claim of 1985, including the allegations that, whenever possible, all weekends were spent in Sparta in the year 1986 and petitioners considered Sparta to be home in 1986. Yet Mr. Smith also claimed that between 1986 and 1991, he did not consider himself a resident of any of the 50 United States, but rather a resident of St. Croix. However, this testimony was also contradicted by the fact that petitioners owned no place of abode on St. Croix for the first three years (1985 - 1987) they originally claimed to have been domiciled there. Petitioners purchased the Green Cay property in August 1985 without a building on it and it was established that they never resided there. The Annas Hope property was purchased in April 1986 with rental units on it, but petitioners never resided in them. Petitioners first occupied the house they built at Annas Hope, St. Croix in November 1987. Thus they were without a house to live in during the years 1985, 1986 and 1987 when they originally claimed to have been domiciled on St. Croix. Although petitioners claimed to have resided in a rental house on their visits to St. Croix prior to the completion of the house, these visits appear to have been more in the nature of a vacation, as indicated by the monthly calendars of petitioners. Finally, petitioners' children attended school in New York City, spent the nonschool part of the year in New Jersey during all of the years at issue, and, at least for the years 1986 through 1989, spent at least twice as much time in New York City as Sparta or St. Croix. This is a pattern of life which speaks to New York City, not Sparta or St. Croix, as petitioners' domicile for the years 1986 through 1991.

Throughout the audit period, petitioners continued to maintain the extensive business ties to New York City that they had prior to 1986. Mr. Smith was the partner-in-charge of the New York City office of Skidmore during the years at issue. Ms. Groh also had a business location in New York City during the audit period, as indicated by various magazine and newspaper articles. The 1986 corporate franchise tax return of GN Design Associates, Inc. stated that GN Design was a New York corporation which began business in 1979. Articles from the August 1987 edition of Working Woman magazine and an article from Business Week in June 1988 both stated that GN Design was located in New York City in 1979. An article in the Washington Post from January 1988 referred to "New York interior designer Carol Groh of GN Associates." Finally, it is noted that throughout the audit period, petitioners were claiming business deductions from their business activities in New York City. "Active" business ties have been considered an indication of a failure to abandon a New York domicile (see, Matter of Kartiganer, Tax Appeals Tribunal, October 17, 1991, confirmed 194 AD2d 879, 599 NYS2d 312).

Petitioners continuously represented themselves to be residents of New York City during the 1970s, 1980s and early 1990s, especially on various administrative and legal documents, although during the same time they now claim to have been domiciled elsewhere. Petitioners' marriage license listed their residence to be in New York City in 1976. In 1977 and again in 1981, their sons' birth certificates listed their legal address to be New York City. The deed purchasing the Sparta house in December 1982 indicated New York City to be their legal residence. Throughout the audit period, the address of record for the children with The Allen-Stevenson School was their New York City apartment. Furthermore, other important documents were mailed to petitioners at their New York City address.

The Appellate Division, Third Department has recently held in Buzzard v. Tax Appeals Tribunal (205 AD2d 852, 613 NYS2d 294) that a most significant factor in determining whether an individual has established a change of domicile to another jurisdiction is the number of days the individual has spent in New York as compared to the number of days spent in the

other jurisdiction. Such a comparison for the days spent in New York City, Sparta and St. Croix by petitioners during the years 1986 through 1989 is shown below. Information for the years 1990 and 1991 was not presented. The New York days include only those days admitted by petitioners to have been spent in New York and the days in which documentation placed petitioners in New York, although petitioners claimed to have been elsewhere. The Sparta and St. Croix days include the days asserted by petitioners to have been spent in each of those jurisdictions less any days in which documentation placed them elsewhere.

	NEW YORK	SPARTA	ST. CROIX
Mr. Smith:			
1986	138	59	64
1987	168	48	67
1988	150	60	61
1989	158	51	53
Ms. Groh:			
1986	158	80	50
1987	150	68	71
1988	140	82	42
1989	148	77	25

For the years 1990 and 1991, a comparison for the days spent by Mr. Smith in New York, Sparta and St. Croix as indicated in the audit report is shown below:

	New York	Sparta	St. Croix
1990	126	69	57
1991	143	84	38

As can be seen by the above figures, petitioners spent at least twice as much time in New York as they did in either Sparta or St. Croix during the years 1986 through 1989. In 1990 and 1991, Mr. Smith spent at least twice as much time in New York as he spent in St. Croix, his claimed place of domicile. For some of the years at issue, petitioners spent three times as many days in New York as they spent in either of the other two jurisdictions. This breakdown of petitioners' whereabouts during each of these years strongly suggests that petitioners did not change their domicile to Sparta or St. Croix, and also strongly suggests that petitioners did not give up their domicile in New York. Furthermore, no information was presented which indicated that petitioners' general pattern of life was any different in 1990 and 1991 than in 1986 through

1989. In fact, the breakdown of the days for 1990 and 1991 for Mr. Smith is consistent with the breakdown for the earlier years. The breakdown also established that the monthly calendars prepared by petitioners for the years 1986 through 1989 are less than accurate. The signed receipts which indicated petitioners were in New York City when they claimed to be elsewhere also contradicted petitioners' claims as to the amount of time they spent in Sparta on the weekends, the amount of time Ms. Groh spent in Fairfield, Connecticut and the claim that when taking a trip by airplane, petitioners always went directly from Sparta to the airport and from the airport to Sparta. Besides tarnishing the testimony of petitioners, they reduced the weight to be given to the affidavits whose purpose were to support petitioners' claimed whereabouts during the years at issue.

Petitioners' retention of title to real property in New York City (Matter of Chrisman, 43 AD2d 771, 350 NYS2d 468; Matter of Roth, Tax Appeals Tribunal, March 2, 1989), continued maintenance of a New York City apartment (Matter of Cooper v. State Tax Commn., 82 AD2d 950, 441 NYS2d 30), and considerable time spent working in New York City during the years at issue (Matter of Clute v. Chu, 106 AD2d 841, 484 NYS2d 239; Matter of Simon, Tax Appeals Tribunal, March 2, 1989) are other factors adverse to petitioners' attempt to establish themselves as domiciliaries of New Jersey and St. Croix during the years 1986 through 1991.

Finally, it is noted that there are numerous other factors which tend to show that petitioners did not change their domicile from New York. These factors include: petitioners' checking and mortgage accounts in New York City banks; petitioners' children attending school in New York City; petitioners' receipt of important documents at their New York City apartment and their childrens' nanny residing in New York City.

It is impossible to find a change of domicile based on the record herein. The facts indicating that petitioners did not change their domicile from New York, when taken together with the numerous occasions that petitioners' testimony was inconsistent with documentation in the record, affords such testimony little consideration in the determination of the issues and severely hinders petitioners in this matter. Petitioners have failed to carry their burden of

establishing by clear and convincing evidence that they intended to change their domicile from New York (State and City) to New Jersey and St. Croix during the years 1986 through 1991.

K. Even if it were to be concluded that petitioners were not domiciled in New York during the years 1986 through 1989, they would be properly assessed herein if they maintained a permanent place of abode within New York and spent in the aggregate more than 183 days there during the years 1986 through 1989 (Tax Law § 605[former (a)(2)]; [b][1][B]). The Division has conceded that petitioners spent fewer than 184 days in New York State and City during 1990 and 1991.

A "permanent place of abode" includes "a dwelling place permanently maintained by the taxpayer, whether or not owned by him" (20 NYCRR 102.2[e][1]). There is no requirement that the petitioner actually dwell in the abode, but simply that he maintain it (see, Matter of Smith v. State Tax Commn., 68 AD2d 993, 994, 414 NYS2d 803). Here, petitioners owned and maintained an apartment in New York City, located at 175 East 62nd Street, throughout the audit period. Petitioner had a telephone listing at the apartment since 1978. Therefore, this apartment constituted a "permanent places of abode" within the meaning of Tax Law § 605(former [a][2]; [b][1][B]).

The remaining issue then is whether petitioners spent in the aggregate more than 183 days of the taxable year in New York. It is concluded that petitioners have failed in their burden to prove that they did not (Tax Law § 689[e]; 20 NYCRR 3000.10[d][4]).

L. In determining whether the petitioners have met their burden of establishing that they spent fewer than 184 days in New York State and City during the years at issue, review was made of the calendars presented by petitioners, the backup documentation, the testimony of petitioners and the evidence introduced at the hearing to establish the various expenses claimed by petitioners. It is noted with regard to this last item that each petitioner had his or her own charge accounts and when it is noted that a credit card sale was made, it is the individual under discussion whose signature appeared on the charge slip.

There are several recurring items within this issue that will be briefly discussed herein

prior to dealing with the individual years. Petitioners claimed in their testimony that the procedure followed when they travelled was to always go directly from Sparta to the airport or train station and upon returning from the trip to go directly from the airport or train station to Sparta. However, as indicated in Finding of Fact "45", there are numerous weekdays on which purchases were made in New York City by either Mr. Smith or Ms. Groh on the date of departure or arrival from a trip taken outside New York State and City. As a result of these discrepancies, all "travel days" were considered New York State and City days where the trip originated or ended in New York City. Petitioners claimed to have been outside of New York City and State for numerous days each year, but submitted no documentation to substantiate this claim. As petitioners have the burden of proof on this issue and submitted nothing to substantiate their claim, these days were also counted as New York State and City days. These days include the days claimed by Ms. Groh to have been spent in Fairfield, Connecticut. In fact, as indicated in Finding of Fact "47", there were days claimed by Ms. Groh to have been spent in Fairfield but where a signed American Express receipt placed her in New York City. It is noted that for the 252 days claimed to have been spent in Fairfield by Ms. Groh over the 4-year period, not one piece of documentation was offered establishing Ms. Groh's presence there. It is concluded that as a result of the discrepancies that existed in the record between the testimony of petitioners and the affidavits presented by them with various documents introduced into the record, the testimony and affidavits were given little weight in the determination of the number of days spent by petitioners in New York State and City during the years 1986 through 1989. Finally, it is observed that the days claimed to have been spent in Sparta but for which no documentation was presented could also be counted as New York days. However, this issue was not addressed as the total of the other types of days exceeded 183, and there is some indication in the record that at least some weekends, especially during the warmer months, were spent in Sparta.

M. For the year 1986, Mr. Smith had 46 travel days, 32 days claimed to have been spent outside New York State but without supporting documentation and 121 days admitted to have

been spent in New York. In addition, there were 17 days where Mr. Smith claimed to have been out of the State, but receipts indicated he was in New York City. Mr. Smith claimed to have been in Hartford, Connecticut on 6 of these 17 days, and in Sparta on 5 of these days. Of the 5 Sparta days, 4 were weekend days, in contrast to petitioners' claim that all weekends were spent in Sparta.

For the year 1987, Mr. Smith had 52 travel days, 23 days claimed to have been spent outside New York State but without supporting documentation and 118 days admitted to have been spent in New York. In addition, the documentation presented by petitioners to substantiate certain business expenses revealed discrepancies between the monthly calendar and the receipts for 50 days where Mr. Smith claimed to be out of State but the receipts indicated his presence within the State. Mr. Smith claimed to have been in Hartford, Connecticut for 16 of the 50 days, and in Sparta for 5 of those days. Of the 5 days, 3 were weekend days.

For the year 1988, Mr. Smith had 41 travel days, 22 claimed non-New York days without backup documentation and 136 days admitted to have been spent in New York. There are, in addition, 14 more days which Mr. Smith indicated on his monthly calendar were spent out of New York State but for which there existed signed American Express receipts indicating his presence within the City. Of these additional 14 days, 13 involved charges made by Mr. Smith either before departing from or after arriving in New York City by airplane. This is in direct contrast to petitioner's testimony that when traveling, he always went directly to the airport from Sparta and directly to Sparta from the airport.

For the year 1989, Mr. Smith had 34 travel days, 24 undocumented days claimed to have been spent outside New York State and 145 days admitted to have been spent in New York. In addition, there are eight days for which an American Express receipt indicated Mr. Smith was in New York City on days he stated were spent in other locations, and five days where other receipts placed Mr. Smith in New York City although his monthly calendar placed him elsewhere. In all, there are four receipts which placed Mr. Smith in New York City on weekends when he claimed to be in Sparta.

N. One recurring item not relevant to Mr. Smith was involved in the determination of Ms. Groh's day count both within and without the State. It involved the number of days claimed to have been spent in Fairfield, Connecticut during the year but for which no substantiation was provided. In addition, numerous days claimed by Ms. Groh to have been spent in Fairfield are contradicted by American Express receipts signed by Ms. Groh indicating that she was in New York City that particular day. Therefore, as petitioners have the burden of proving that they spent less than 184 days in New York City and State during the years at issue, and no documentation was presented as to Ms. Groh's claim of days spent in Fairfield, Connecticut, the days claimed to have been spent in Fairfield will be counted as New York days.

For the year 1986, Ms. Groh had 26 travel days, 60 Fairfield days and 141 days admitted to have been spent in New York City. Furthermore, there were 17 days which were claimed to have been spent outside of New York, but American Express receipts signed by Ms. Groh established that she was in New York City on those days. Of the 17 days, 9 were claimed to have been spent in Fairfield and 5 were claimed to have been spent in Sparta on weekend days.

For the year 1987, Ms. Groh had 28 travel days, 63 Fairfield days and 144 days admitted to have been spent in New York City. There were, in addition, six days with American Express receipts indicating Ms. Groh was in New York City when her monthly calendar indicated she was outside the State. Of the six days, two were claimed to have been spent in Fairfield and three were claimed to have been spent in Sparta on weekend days.

For the year 1988, Ms. Groh had 27 travel days, 65 Fairfield days and 137 days admitted to have been spent in New York City. There are three additional days for which there existed documentation that established that Ms. Groh was in New York City on those days.

For the year 1989, Ms. Groh had 37 travel days, 64 Fairfield days and 145 days admitted to have been spent in New York City. There are three additional days for which there existed documentation that established that Ms. Groh was in New York City on those days.

O. Based upon the documents in the record, the lack of documentation in the record as to the days claimed to have been spent outside the State and the lack of credibility afforded

petitioners' testimony due to the numerous contradictions in the record, it is clear that petitioners have failed to meet their burden of establishing that they spent less than 184 days in New York City during the years 1986 through 1989.

P. Petitioners contend that the absence from the hearing of the individuals who conducted the audits for the years 1988 through 1991 deprived them of their fundamental rights to due process and to confront their accusers. This contention is rejected. The Division of Taxation is not required to produce the auditor who conducted the audit (see, Matter of Mira Oil Co. v. Chu 114 AD2d 619, 494 NYS2d 458, lv denied 68 NY2d 602, 505 NYS2d 1026; Matter of Array Service, Inc., Tax Appeals Tribunal, December 1, 1988).

Furthermore, petitioners contend that the notices of deficiency relating to the years 1988 through 1991 are not supported by "substantial evidence" within the meaning of State Administrative Procedure Act § 306(1) and therefore must be cancelled. Petitioners argue that because the auditors involved in the years 1988 through 1991 were not subject to cross-examination, and the hearsay audit reports were the only evidence to support the notices of deficiency, those notices must be cancelled. This contention is also rejected. State Administrative Procedure Act § 306(1) provides, in part, as follows:

"No decision, determination or order shall be made except upon consideration of the record as a whole or such portion thereof as may be cited by any party to the proceeding and as supported by and in accordance with substantial evidence. . . ."

It is initially noted that the substantial evidence requirement of section 306(1) applies to the determination as a whole and not to each individual document introduced into the record. Furthermore, not only is hearsay admissible in administrative proceedings, it may even serve as the basis for the administrative determination (see, Matter of EJG Corp. v. State Liquor Authority, 213 AD2d 924, 624 NYS2d 68; Matter of Gray v. Adduci, 73 NY2d 741, 536 NYS2d 40). Moreover, while not the case herein, the determination "may consist entirely of hearsay evidence" (Matter of Hirsch v. Corbisiero, 155 AD2d 325, 548 NYS2d 1, 2, lv denied 75 NY2d 708, 555 NYS2d 691).

While an assessment of tax must have a rational basis (see, Matter of Donahue v. Chu,

104 AD2d 523, 479 NYS2d 889, 892), the Division does not have an affirmative burden to establish the rational basis for its assessment (see, Matter of Metzger, Tax Appeals Tribunal, February 11, 1993). Rather, a presumption of correctness attaches to an assessment issued by the Division which, in itself, provides the rational basis, so long as no evidence is introduced challenging the assessment (Matter of Leogrande v. Tax Appeals Tribunal, 187 AD2d 768, 589 NYS2d 383, lv denied 81 NY2d 704, 595 NYS2d 398; see, Matter of Tavalacci v. State Tax Commn., 77 AD2d 759, 431 NYS2d 174). In the present matter, the field audit report, the audit workpapers, the documentation obtained by the auditors from petitioners and petitioners' personal income tax returns for the years at issue are sufficient to allow a trier of fact to determine that the audits and the resulting notices of deficiency had a rational basis (see, Matter of Grecian Square v. State Tax Commn., 119 AD2d 948, 501 NYS2d 219).

Q. Section 170 of the Internal Revenue Code allows individuals a deduction for charitable contributions subject to certain limitations. In general, charitable contributions may be substantiated by a cancelled check, a receipt or a reliable written record setting forth the name of the donee, the date of the contribution and the amount of the contribution (Treas Reg § 1.170A-13). For the year 1986, petitioners have established through the introduction of copies of cancelled checks issued to The Allen-Stevenson School and letters from the school acknowledging the gifts from petitioners that they made contributions to the school of \$2,500.00 (check, letter and publication), \$40.05 (check), \$500.00 (letter) and \$10,000.00 (letter), for a total of \$13,040.05. For the year 1987, petitioners have established that they donated \$2,500.00 (check) to the school's annual fund drive. The testimony of Mr. Smith as to the remaining two cancelled checks totalling \$6,000.00 was too vague to establish the reason why the checks were given to the school and certainly did not establish that the money was donated as a charitable contribution. As no documentation was offered as to the amounts claimed to have been donated to the Christ Church for either year, these amounts are disallowed. In conclusion, petitioners are entitled to charitable contribution deductions relating to the amounts originally claimed to have been donated to The Allen-Stevenson School and the

Christ Church of \$13,040.05 in 1986 and of \$2,500.00 in 1987.

R. Section 165(a) of the Internal Revenue Code allows a deduction for any loss sustained during the taxable year and not compensated for by insurance. Section 165(c)(3) limits the deduction to losses of property where such losses arise from fire, storm, shipwreck, or other casualty. Petitioners have established through the introduction of repair invoices that the cost of the repairs to the rental units on St. Croix was \$798,839.00 and the cost of the repairs to their residence on St. Croix was \$945,750.00 as a result of the damage caused by Hurricane Hugo. Insurance coverage as indicated by checks and correspondence from the insurance companies was \$353,598.00 toward the losses sustained by the rental units and \$765,000.00 toward the losses sustained by the residence, resulting in net casualty losses of \$445,241.00 and \$180,750.00 for the rental units and residence, respectively. Petitioners are entitled to deduct these net casualty losses in the year 1989.

S. Petitioners are entitled to the passive losses computed on their Federal Form 8582 and claimed on their Federal Schedule E for the years 1988 and 1989, as permitted by Internal Revenue Code § 469. This issue was all but conceded by the auditor when he told petitioners' representative by telephone and by letter that the full passive losses for both years should have been allowed.

T. Petitioners claimed a capital loss under Internal Revenue Code § 1231 upon the sale of 848 shares of stock held in a cooperative apartment at 212-214 East 77th Street during 1987. Section 1001(a) of the Internal Revenue Code states, as follows:

"The gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the adjusted basis provided in section 1011 for determining gain, and the loss shall be the excess of the adjusted basis provided in such section for determining loss over the amount realized."

Under section 1011(a), the adjusted basis for determining the gain or loss from the sale of property shall be the basis determined pursuant to section 1012. Section 1012 provides that the basis of property shall be the cost of such property. In order to establish the claimed loss on the sale of the 848 shares, it was necessary for petitioners to establish the basis, or cost, of the property. During the course of the hearing petitioners had in their possession the original

closing statement relating to the purchase of the building in 1981. This document would have adequately addressed the question of the basis of the property at issue. However, petitioners chose not to introduce the original closing statement into evidence and this failure must be viewed in a light most unfavorable to petitioners. Therefore, petitioners have failed to substantiate the basis and thus establish their entitlement to the claimed capital loss on the sale of the 848 shares of stock held in the cooperative apartment located at 212-214 East 77th Street in 1987.

U. Internal Revenue Code § 162 provides for deductions for all ordinary and necessary expenses incurred during the taxable year in carrying on any trade or business. To qualify as allowable trade or business expense deductions under section 162(a), the item must (1) be "paid or incurred during taxable year," (2) be for "carrying on any trade or business," (3) be an "expense," (4) be a "necessary" expense, and (5) be an "ordinary" expense (Commissioner v. Lincoln Sav. & Loan Asso., 403 US 345, 29 L Ed 2d 519).

Addressing the issue of the ordinary and necessary business expenses claimed by petitioners for the year 1986, petitioners have submitted sufficient documentation in the form of checks and charge card summaries to be entitled to claim the following expenses on their Statement 1 for 1986:

Office supplies	\$8,751.00
Labor	6,919.00
Travel	5,187.00
Entertainment	7,669.00
Maintenance	3,350.00

The subscription expense of \$2,821.00 is to be reduced by the amount of the four checks (\$468.00) which appear as substantiation here as well as in labor expenses. The claim for utility expenses of \$185.00 and telephone expenses of \$192.00 are denied in full as they do not appear to be related to a trade or business and are personal or living expenses, relating to the house in New Jersey (see, IRC former § 262). As to the New York telephone expenses, it was incumbent upon petitioners to establish a reasonable allocation of the charges between personal and business use; without such an allocation no deduction can be allowed (see, International

Trading Co. v. Commissioner, 275 F2d 578).

As to the Statement 2 expenses on the 1986 return, petitioners have established through charge card statements and cancelled checks entitlement to the following business expenses:

Entertainment	\$15,317.00
Maintenance	30,151.00
Travel	16,932.00

Claimed office supplies expenses of \$81,087.00 are properly reduced by \$4,248.00, which includes checks to the Sparta housecleaner, a personal expense, and the six checks which were not cashed by any banking institution. The claimed professional expenses of \$8,017.00 are to be reduced by \$2,592.00, which is the amount of the check not cashed. In addition, the labor expenses of \$32,015.00 should be reduced by the amount of the seven checks which appear twice in the exhibit, or \$3,826.00. The utility expenses which include personal items relating to the Sparta house and other items which could relate to both personal and business items but which petitioners have not allocated, the insurance expenses which are not allocated between business and personal and which also, on their face, could be personal in nature and the miscellaneous expenses which are documented by cash register receipts which do not identify the items purchased, are all denied in full.

For the year 1987, petitioners were able to substantiate through the introduction of charge statements, cancelled checks and expense statements from Skidmore the following business deductions and amounts:

Supplies	\$20,285.00
Professional fees	14,489.00
Mortgage	14,268.00
Entertainment	25,293.00
Travel	27,171.00
Cleaning & Maintenance	7,506.00
Maintenance	30,238.00

The expenses claimed for office supplies are denied in full. Many of the checks submitted are clearly for expenses not properly deductible as business expenses and/or not properly included in this category. Some of the checks were for expenses incurred at the Sparta house and others appear to be for other personal items. Without the invoices to verify the purpose or item

purchased, the remaining items must also be disallowed. The utility expenses are disallowed in full as they relate either to the Sparta house or to the New York apartment without a proper allocation between personal and business use. The latter rationale applies to the disallowance of the insurance expenses as well. In addition, one insurance check was not cashed by a banking institution. The expense for labor must be disallowed because of an accumulation of deficiencies in the documentation presented. The checks presented contained thirteen which were not cashed, ten addressed to the Sparta housecleaner and two which appear twice. The inclusion of these obviously incorrect documents brings into question the remaining checks, and without an explanation of the recipients and how they are related to petitioners' businesses, they are also disallowed. The miscellaneous expenses are also disallowed in full as the cash register tapes, in the main, do not identify the items purchased, and the items that are identified appear to be personal in nature.

For the year 1988, petitioners submitted sufficient documentation in the form of cancelled checks to be entitled to the business deduction for the following expenses:

Professional Fees	\$95,616.00
Payroll & other taxes	3,500.00

The documentation for the office supplies expense included items that are personal in nature and receipts that do not identify the items purchased. There are also checks written to American Airlines, GN Associates and the Connecticut Broadcasting Co. which do not appear, without explanation, to relate to office supplies. Without any explanation of the items purchased and the purpose of the items, the office supplies expense is disallowed in full. A similar rationale applies to the claimed supplies expenses. Many of the checks are written to companies or individuals which clearly did not provide supplies to petitioners' business operations, including: the Buccaneer Bay Landowners Assoc., the Morgan-Francis Co. which sold the flagpole for the St. Croix property, Fisher Skylights which contracted to do the lighting in the St. Croix house, K. Robert Najarian, Ms. Groh's partner in GN Design, and A & S Landscaping. Without an explanation as to how these and the remaining expenses relate to petitioners' business activities, the supplies expense is denied in full. The utility expenses are denied in full as the expenses are

either personal in nature, as they relate to the Sparta or St. Croix property or are not properly allocated between business and personal use. There are twelve checks written to "Madelyn Simon" totalling \$3,045.00 which are not accompanied by an explanation as to her relationship to the utilities which were provided. The insurance expense deduction fails for want of information. Of the five different insurance companies for which checks were presented, one insured the St. Croix property and another the Sparta house. There was no information provided as to the remaining three companies and therefore all such expenses are denied in full. The labor expenses are denied in full due to the 15 checks which were presented in support of other expense categories as well, the 9 checks written to the Sparta housekeeper and the lack of any explanation as to who the payees were and what services they performed for petitioners.

Petitioners submitted sufficient documentation in the form of credit card statements, invoices, checks and Skidmore expense statements to establish entitlement to the following expenses claimed for the year 1989:

Business	\$35,213.00
Publications	3,983.00
Maintenance & Repair	13,505.00
Professional Fees	11,932.00
Supplies	11,026.00
Payroll Taxes	2,166.00

Petitioners' claimed transportation expenses of \$40,828.00 are to be reduced by the three uncashed checks addressed to Skidmore, totalling \$9,097.00. The amount of the fourth Skidmore expense statement, in the amount of \$1,395.00, is also disallowed as there is an obvious pattern of Mr. Smith's not having reimbursed Skidmore for the expenses shown on its statements in this year. The meals and entertainment expenses in the amount of \$28,114.00 are to be reduced by the adding machine tape totals of \$24,926.00 as there is no original source documentation supporting the amount claimed and by the Skidmore expense statement in the amount of \$1,798.00 as there is no proof of its having been paid. Such expense remaining is \$1,112.00 ($\$1,390.00 \times 80\%$). The office supplies expense of \$15,711.00 is to be reduced by \$7,957.00, which represents the checks not cashed by a banking institution, including those written to cover the Skidmore expense statements. Miscellaneous expenses of \$1,594.00 are to

be reduced by \$575.00, which is the amount of the check written to the Lake Mohawk Club and not documented as a business expense. Advertising expenses of \$950.00 are to be reduced by \$360.00, which is the amount of the four checks which clearly were not written for advertising (one check written for "pillowcovers-kware", one to Woolworth and two to Bloomingdales).

Petitioners submitted checks and other documentation to support their claimed expenses for the year 1990 as follows:

Maintenance	\$45,357.00
Publications & Supplies	1,739.00
Miscellaneous	666.00
Professional Fees	23,559.00
Meals & Entertainment	5,774.00

Labor expenses of \$40,913.00 are to be reduced by the checks written to the Sparta housekeeper and the children's nanny, neither of whose services were performed for petitioners' business ventures. Petitioners' testimony that the nanny performed clerical services is not credible. In addition, no proof was offered that the nanny was paid separately for her clerical and child supervision services. These checks totalled \$18,940.00. Business expenses are to be reduced by the amount of the uncashed check, \$250.00. Claimed transportation expenses in the amount of \$16,548.00 were supported by checks, credit card statements, credit card receipts and travel agency receipts. All the expenses are properly documented except for the uncashed check in the amount of \$465.00, which is to be eliminated from the amount claimed. The telephone expenses claimed are denied in full. No allocation was made as to those expenses which could possibly be business expenses but also have the potential to be personal expenses. Without such an allocation, it is impossible to determine which New York telephone expenses are related to petitioners' businesses. No explanation was provided as to how the New Jersey expenses were related to the New York businesses. The insurance expenses are denied in full as no explanation was provided as to what these companies insured and therefore their relationship, if any, to the business activities of petitioners. The claimed utility expenses are denied in full as the payees do not in any way appear to be providers of utility services.

Petitioners produced sufficient documentation to be entitled to the following expenses

claimed for the year 1991:

Maintenance	\$46,524.00
Publications & Supplies	957.00
Plants & Maintenance	3,594.00

Checks in the amount of \$9,566.00 which were not cashed by any banking institution are to be removed from the amount claimed as professional expenses. The transportation expenses allowed are to be reduced to \$4,239.00, eliminating the claimed expenses documented only by adding machine tapes and handwritten notations as they provide no source documentation for these expenses. Cleaning expenses of \$5,146.00 are to be reduced by the checks written to the Sparta housekeeper, totalling \$760.00. Repair expenses are to be reduced by the amount of the check written to Sparta Electric, \$432.00, as no explanation was provided as to the relation of this obvious personal expense to petitioners' business operations. The claimed office supplies expense of \$9,028.00 is to be reduced by \$2,286.00, which is the amount of the expense substantiated only by adding machine tapes and without original source documentation. The labor, telephone, insurance and meals and entertainment expenses are denied in full. The labor expenses are supported only by checks and a Federal form 1099 issued to petitioners' nanny, a personal expense. The telephone and insurance expenses were not allocated between possible business and personal expenses. Finally, the meals and entertainment expenses are not supported by original source documentation but only adding machine tapes which do not identify the items purchased.

An examination of the documentation submitted in support of the business expenses claimed by petitioners for their business ventures revealed a willingness upon the part of the petitioners to employ less than straightforward methods in their attempts to substantiate the amount of the expenses claimed. Petitioners continuously and consistently claimed as expenses of their New York office the utility and telephone expenses of their Sparta house, the cost of their housekeeper in Sparta, the cost of their nanny and the amounts indicated on checks which were not cashed by any banking institution. In addition, they frequently claimed the same expenses more than once.

V. It is noted that since petitioners have been determined to be domiciliaries of New York State, they are not entitled to any business expenses listed on their Federal Schedule A under the following categories; maintenance, plants and plant maintenance, telephone, insurance, cleaning, repairs, utilities, office supplies, general supplies and miscellaneous expenses as they relate to the apartment located at 175 East 62nd Street.

W. Pursuant to Internal Revenue Code § 163(a), a taxpayer may generally deduct interest paid within the tax year on indebtedness. However, a taxpayer not a corporation may not deduct personal interest paid during the taxable year (IRC § 163[h][1]). The term "personal interest" does not include investment interest (IRC § 163[h][2][B]). The deduction by a noncorporate taxpayer for interest on investment indebtedness is limited to the taxpayer's net investment income (IRC § 163[d]). Net investment income is the excess of investment income over investment expenses.

Petitioners have established that they paid and claimed \$140,544.00 in investment interest in 1988 and \$71,990.00 in investment interest in 1989. As petitioners' net investment income in both years exceeded the amount claimed, they are entitled to the investment interest deduction as claimed in the years 1988 and 1989.

X. Penalties were imposed herein pursuant to Tax Law § 685(b) and (p). Petitioners have failed to articulate any rationale for the abatement of such penalties. Under such circumstances and considering the discrepancies that existed between petitioners' claimed days outside of New York State and City and the documentation which established otherwise, the discrepancies that existed between the claimed expenses and deductions and the documentation presented, the numerous contradictions between the testimony and the documents and the use of certain items as deductions when they clearly were not, penalties imposed herein are properly sustained.

Y. In summary, petitioners have established entitlement to the following items for the years indicated: The total business expenses are based upon petitioners' being determined domiciliaries of New York State for the years 1986 through 1991 (see, Conclusion of Law "V").

For 1986:
charitable contributions of \$13,040.05.
total business expenses of \$22,128.00 for statement 1.
total business expenses of \$65,863.00 for statement 2.

For 1987:
charitable contributions of \$2,500.00.
total business expenses of \$66,953.00.

For 1988:
passive losses of \$47,782.00.
total business expenses of \$99,116.00.
investment interest expense of \$140,544.00.

For 1989:
passive losses of \$148,104.00
total business expenses of \$85,332.00.
investment interest expense of \$71,990.00.
net casualty losses of \$625,991.00.

For 1990:
total business expenses of \$85,926.00.

For 1991:
total business expenses of \$57,047.00.

In the alternative, if petitioners had been determined to be nondomiciliaries of New York, they would have been entitled to the following business expenses:

<u>Year</u>	<u>Amount</u>
1986 - statement 1	\$ 34,599.00
1986 - statement 2	172,859.00
1987	139,250.00
1988	99,116.00
1989	118,636.00
1990	131,949.00
1991	118,293.00

Z. The petitions of Carol A. Groh and Donald C. Smith are granted as indicated in Conclusion of Law "Y"; the notices of deficiency issued February 15, 1991 and October 13, 1994 are modified accordingly and except as so granted the petitions are denied.

DATED: Troy, New York
May 8, 1997

/s/ Thomas C. Sacca
ADMINISTRATIVE LAW JUDGE